



DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Parts 1005, 1006 and 1007

[AMS-DA-07-0059; AO-388-A22; AO-356-A43 and AO-366-A51; Doc. No. DA-07-03]

Milk in the Appalachian, Florida and Southeast Marketing Areas; Final Decision on Proposed Amendments to Marketing Agreements and to Orders.

AGENCY: Agricultural Marketing Service, USDA

ACTION: Proposed rule.

SUMMARY: This final decision proposes to permanently adopt amendments that adjust the Class I pricing surface of the Appalachian, Florida, and Southeast Federal milk marketing orders. In addition, this decision seeks to adopt proposals that amend certain features of the diversion limit, touch-base, and transportation credit provisions for the Appalachian and Southeast milk marketing orders. This decision also proposes to adopt amendments that increase the maximum administrative assessment for the Appalachian, Florida and Southeast marketing orders. The orders as amended are subject to approval by producers in the affected markets. Producer approval for this action will be determined concurrently with amendments adopted in a separate final decision that amends the transportation balancing fund and other provisions of the Appalachian and Southeast milk marketing orders.

FOR FURTHER INFORMATION CONTACT: Erin Taylor, USDA/AMS/Dairy Programs, Order Formulation and Enforcement Branch, STOP 0231-Room 2971, 1400 Independence Avenue, SW, Washington, DC 20250-0231, (202) 720-7311, e-mail address: erin.taylor@ams.usda.gov.

SUPPLEMENTARY INFORMATION: This final decision adopts amendments that:

1) Adjust the Class I pricing surface in the Appalachian, Florida, and Southeast marketing orders; 2) Make diversion limit standards identical for the Appalachian and Southeast orders: 25 percent of deliveries to pool plants during the months of January, February, July, August, September, October, and November, and 35 percent in the months of March, April, May, June, and December; 3) Reduce touch-base standards to one day each month for the Appalachian and Southeast orders; 4) Add January and February as months when transportation credits are paid for the Appalachian and Southeast orders; 5) Provide for the payment of transportation credits in the Appalachian and Southeast orders for full loads of supplemental milk; 6) Provide more flexibility in the qualification requirements for supplemental milk producers to receive transportation credits for the Appalachian and Southeast orders; and 7) Increase the monthly transportation credit assessment from \$.20 per hundredweight (cwt) to \$0.30 per cwt in the Southeast order. This decision also increases the maximum administrative assessment for the Appalachian, Florida, and Southeast orders from \$0.05 per cwt to \$0.08 per cwt. Increasing the maximum administrative assessment was initially addressed in a separate recommended decision (73 FR 11062). Comments concerning the recommended decision were requested but none were received. Accordingly, this document is the final decision on all proposals addressed in both the tentative final decision (73 FR 11194) for items 1 through 7 above and the recommended decision (73 FR 11062) that were simultaneously published in the Federal Register on February 25, 2008.

This administrative action is governed by the provisions of Sections 556 and 557 of Title 5 of the United States Code and, therefore, is excluded from the requirements of Executive Order 12866.

The amendments to the rules proposed herein have been reviewed under Executive Order 12988, Civil Justice Reform. They are not intended to have a retroactive effect. If adopted, the amendments would not preempt any state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule.

The Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601-674) (AMAA), provides that administrative proceedings must be exhausted before parties may file suit in court. Under Section 608c(15)(A) of the AMAA, any handler subject to an order may request modification or exemption from such order by filing a petition with the Department of Agriculture (USDA) stating that the order, any provision of the order, or any obligation imposed in connection with the order is not in accordance with the law. A handler is afforded the opportunity for a hearing on the petition. After a hearing, USDA would rule on the petition. The AMAA provides that the district court of the United States in any district in which the handler is an inhabitant, or has its principal place of business, has jurisdiction in equity to review USDA's ruling on the petition, provided a bill in equity is filed not later than 20 days after the date of the entry of the ruling.

Regulatory Flexibility Act and Paperwork Reduction Act

In accordance with the Regulatory Flexibility Act (5 U.S.C. 601-612), the Agricultural Marketing Service has considered the economic impact of this action on small entities and has certified that this proposed rule would not have a significant economic impact on a substantial number of small entities. For the purposes of the

Regulatory Flexibility Act, a dairy farm is considered a small business if it has an annual gross revenue of less than \$750,000 and a dairy products manufacturer is a small business if it has fewer than 500 employees.

For the purposes of determining which dairy farms are small businesses, the \$750,000 per year criterion was used to establish a marketing guideline of 500,000 pounds per month. Although this guideline does not factor in additional monies that dairy producers receive, it should be an inclusive standard for most small dairy farmers. For purposes of determining a handler's size, if the plant is part of a larger company operating multiple plants that collectively exceed the 500-employee limit, the plant will be considered a large business even if the local plant has fewer than 500 employees.

During May 2007, the time of the hearing, there were 2,744 dairy farmers pooled on the Appalachian order (Order 5), 2,924 dairy farmers pooled on the Southeast order (Order 7), and 283 dairy farmers pooled on the Florida order (Order 6). Of these, 2,612 dairy farmers in Order 5 (or 95 percent), 2,739 dairy farmers in Order 7 (or 94 percent), and 153 dairy farmers in Order 6 (or 54 percent) were considered small businesses.

During May 2007, there were a total of 36 plants associated with the Appalachian order (22 fully regulated plants, 10 partially regulated plants, 2 producer-handlers, and 2 exempt plants). A total of 55 plants were associated with the Southeast order (33 fully regulated plants, 9 partially regulated plants, 2 producer-handlers, and 11 exempt plants). A total of 25 plants were associated with the Florida order (13 fully regulated plants, 9 partially regulated plants, 1 producer-handler, and 2 exempt plants). The number of plants meeting small business criteria under the Appalachian, Southeast, and Florida orders were 8 (or 22 percent), 18 (or 33 percent), and 11 (or 44 percent), respectively.

The adopted amendments in this final decision provide for an increase in Class I prices in the Appalachian, Southeast, and Florida orders. The minimum Class I prices of the three southeastern orders, as with all other Federal milk marketing orders, are set by using the higher of an advance Class III or Class IV price as determined by USDA and adding a location-specific differential, referred to as a Class I differential. Minimum Class I prices charged to regulated handlers are applied uniformly to both large and small entities. At the time of the hearing, the Department estimated that the proposed Class I price increases would generate higher marketwide pool values in all three southeastern orders of approximately \$18-19 million for the Appalachian order, \$17.5 million for the Southeast order, and \$38 million for the Florida order, on a monthly basis. It was estimated that monthly minimum prices paid to dairy farmers (blend prices) would increase approximately \$0.26 per cwt for the Appalachian order, \$0.64 per cwt for the Southeast order, and \$1.20 per cwt for the Florida order.

The Class I price increases were implemented on an interim basis effective May 1, 2008.¹ As a result of those increases, marketwide pool values were increased in 2011 by approximately \$16 million in the Appalachian order, \$38 million in the Florida order, and \$16 million in the Southeast order. This resulted in an increase in 2011 monthly minimum prices paid to dairy farms of \$0.25 per cwt for the Appalachian order, \$1.25 per cwt in the Florida order, and \$1.25 per cwt in the Southeast order.

The adopted amendments revise the Appalachian and Southeast orders by making the diversion limit standards for the orders identical – not to exceed 25 percent in each of the months of January, February, and July through November, and 35 percent in each of the months of March through June and for the month of December. Prior to their interim

¹ 73 FR 14153

adoption, the diversion limit standards of the Appalachian order for pool plants and cooperatives acting as handlers were not to exceed 25 percent in each of the months of July through November, January, and February; and 40 percent in each of the months of December and March through June. For the Southeast order, prior to their interim adoption, the diversion limit standards for pool plants and cooperatives acting as handlers were not to exceed 33 percent in each of the months of July through December and 50 percent in each of the months of January through June.

In addition, the adopted amendments establish identical touch-base standards of at least one day's milk production every month for a dairy farmer in the Appalachian and Southeast orders. Prior to their interim adoption, the Appalachian order had a touch-base standard of 6 days' production in each of the months of July through December and not less than 2 days' production in each of the months of January through June. Prior to their interim adoption, the Southeast order had a touch-base standard of not less than 10 days' production in each of the months of July through December and not less than 4 days' production in each of the months of January through June.

The adopted amendments to the pooling standards serve to revise established criteria that determine those producers, producer milk, and plants that have a reasonable association with and are consistently serving the fluid needs of the Appalachian and Southeast marketing areas. Criteria for pooling are established on the basis of performance levels that are considered adequate to meet the Class I needs and determine those producers who are eligible to share in the revenue that arises from the classified pricing of milk. The criteria for pooling are established without regard to the size of any dairy industry or entity. The established criteria are applied in an identical fashion to

both large and small businesses and do not have any different economic impact on small entities as opposed to large entities.

The adopted amendments add January and February to the months of July through December as months when transportation credits may be paid to those handlers who incur the costs of providing supplemental milk for the Appalachian and Southeast orders. The amendments also expand the payment of transportation credits for supplemental milk to include the full load of milk rather than the calculated Class I portion and provide more flexibility in the qualification requirements for supplemental milk producers to receive transportation credits. In addition, the maximum monthly transportation credit assessment for the Southeast order is increased from \$0.20 per cwt to \$0.30 per cwt on all milk assigned to Class I use. The transportation credit provisions are applicable only to the Appalachian and Southeast orders, are applied in an identical fashion to both large and small businesses, and will not have any different impact on those businesses producing manufactured milk products. The changes will not have a significant economic impact on a substantial number of small entities.

The adopted amendments also allow the Market Administrators of the Appalachian, Southeast, and Florida orders to increase the administrative assessment from the current \$0.05 per cwt to \$0.08 per cwt if necessary to maintain adequate funds for the operation of the orders. Administrative assessments are charged without regard to the size of any dairy industry or entity. Therefore, the proposed amendments will not have a significant economic impact on a substantial number of small entities.

The Agricultural Marketing Service is committed to complying with the E-Government Act, to promote the use of the Internet and other information technologies to

provide increased opportunities for citizen access to Government information and services.

This action does not require additional information collection that needs clearance by the Office of Management and Budget (OMB) beyond currently approved information collection. The primary sources of data used to complete the forms are routinely used in most business transactions. Forms require only a minimal amount of information that can be supplied without data processing equipment or a trained statistical staff. Thus, the information collection and reporting burden is relatively small. Requiring the same reports for all handlers does not significantly disadvantage any handler that is smaller than the industry average.

Interested parties were invited to submit comments on the probable regulatory and informational impact of this proposed rule on small entities.

Prior documents in this proceeding

Notice of Hearing: Issued May 3, 2007; published May 8, 2007 (72 FR 25986).

Partial Tentative Final Decision: Issued February 25, 2008; published February 29, 2008 (73 FR 11194).

Partial Recommended Decision: Issued February 25, 2008; published February 29, 2008 (73 FR 11062).

Interim Final Rule: Issued March 12, 2008; published March 17, 2008 (73 FR 14153).

Correcting Amendments: Issued May 6, 2008; published May 9, 2008 (73 FR 26513).

Preliminary Statement

A public hearing was held upon proposed amendments to the marketing agreement and the orders regulating the handling of milk in the Appalachian, Florida and Southeast

marketing areas. The hearing was held, pursuant to the provisions of the Agricultural Marketing Agreement Act of 1937 (AMAA), as amended (7 U.S.C. 601-674), and the applicable rules of practice and procedure governing the formulation of marketing agreements and marketing orders (7 CFR Part 900).

The proposed amendments set forth below are based on the record of a public hearing held in Tampa, Florida, on May 21-23, 2007, pursuant to a notice of hearing issued May 3, 2007, published May 8, 2007 (72 FR 11194).

Upon the basis of the evidence introduced at the hearing and the record thereof, USDA issued a Tentative Final Decision and a Recommended Decision on February 25, 2008, containing notice of the opportunity to file written exceptions thereto.

The materials issues on the hearing record relate to:

1. Class I Prices – adjustments and pricing surface.
2. Producer milk – diversion limit and touch-base standards.
3. Transportation credit balancing fund provisions.
4. Administrative assessment provisions.

Findings and Conclusions

This final decision proposes to adopt proposals, published in the hearing notice as Proposals 1, 2, 3, 4, 5, and 6, seeking to make various changes to the Appalachian, Southeast, and Florida milk marketing orders (hereinafter these marketing areas and marketing orders will collectively be referred to as the southeastern marketing areas or orders as appropriate). These amendments form a package of changes that simultaneously provide for an increase in Class I prices and the Class I pricing surface in the three southeastern orders; and for the Appalachian and Southeast orders, more

stringent diversion limit standards, lower touch-base standards, and other specific changes to the transportation credit balancing fund provisions. This final decision also adopts proposals, published in the hearing notice as Proposals 4, 5, and 6, for increasing the maximum administrative assessment rate on producer milk from the current \$0.05 per cwt to \$0.08 per cwt for the Appalachian, Southeast, and Florida orders.

While the summary of testimony is presented as four separate material issues, the discussion and findings on all material issues are provided after the summary of comments and exceptions.

The minimum Class I prices of the three southeastern orders, as with all other Federal milk marketing orders, are set by using the higher of an advance Class III or Class IV price as determined by USDA and adding a location-specific differential, referred to as a Class I differential. The Class I differentials are location-specific by county and parish for all States of the 48 contiguous United States. These Class I differentials are specified in 7 CFR Section 1000.52.

The diversion limit standards of the Appalachian and Southeast milk orders are described in the Producer milk definition of the orders (7 CFR 1005.13 and 7 CFR 1007.13, respectively). The standards specify the maximum volume of milk that may be diverted to a nonpool plant and still pooled and priced under each respective order. Prior to their interim adoption, the diversion limit standards of the Appalachian order for cooperatives acting as handlers (and pool plant operators that are not cooperatives) were not to exceed 25 percent in each of the months of July through November and the months of January and February. Those limits changed to 40 percent in each of the months of March through June as well as the month of December. Prior to their interim adoption

for the Southeast order, the diversion limit standards for cooperatives acting as handlers (and pool plant operators that are not cooperatives) were not to exceed 33 percent in each of the months of July through December and 50 percent in each of the months of January through June. As adopted herein, the diversion limit standards of both orders are made identical – not to exceed 25 percent for the months of January, February, and each of the months of July through November, and 35 percent for each of the months of March through June and for the month of December. This represents a modest tightening of the diversion limit standards for the Appalachian order and a significant tightening of the diversion limit standards for the Southeast order.

This decision adopts identical touch-base standards of at least 1 day's milk production per month for a dairy farmer to be considered a producer under each respective order's Producer milk definition and for making a producer's milk eligible for diversion to nonpool plants. This represents a significant change from the touch-base standards for the Appalachian and Southeast orders. Prior to their interim adoption, the Appalachian order touch-base standard was 6 days' production in each of the months of July through December and not less than 2 days' production in each of the months of January through June. For the Southeast order, the touch-base standard was not less than 10 days' production in each of the months of July through December and not less than 4 days' production in each of the months of January through June.

Currently, of the three southeastern orders, only the Appalachian and Southeast orders contain provisions for a transportation credit to partially offset handler costs of transporting supplemental milk for Class I use during certain times of the year from producers located outside of the two marketing areas. These producers are not part of the

regular and consistent supply of Class I milk to the Appalachian and Southeast marketing areas.

Transportation credit balancing funds were first established for the Appalachian and Southeast (or predecessor orders) in 1996 and operate independently of the producer settlement funds. A monthly per cwt assessment is charged to Class I handlers on a year-round basis on the volume of milk assigned to Class I use at a rate of \$0.15 per cwt in the Appalachian order and, prior to its interim adoption, \$0.20 per cwt in the Southeast order. Payments from the transportation credit balancing fund are made during the months of July through December (when milk supplies are tightest) in both orders to those handlers that incur the costs of providing supplemental milk. The transportation credit balancing fund provisions were amended in a separate rulemaking and made effective on an interim basis on December 1, 2006 (71 FR 62377), and were again amended by this rulemaking proceeding on an interim basis effective March 18, 2008 (73 FR 14153).

Changes proposed in this final decision to the Appalachian and Southeast order transportation credit balancing fund provisions continue the previous amendments that were adopted on an interim basis (73 FR 14153). The amendments: 1) extend the number of months that transportation credit balancing funds may be paid from the current months of July through December to include the months of January and February, with the option of the month of June if requested and approved by the market administrator; 2) expand the payment of transportation credits for supplemental milk to include the entire load of milk rather than the current calculated Class I utilization; 3) provide more flexibility in the qualification requirements for supplemental milk producers to receive transportation

credits; and 4) increase the monthly transportation credit assessment rate from the current \$0.20 per cwt to \$0.30 per cwt for the Southeast order.

The final decision also recommends adoption of three proposals published in the hearing notice as Proposals 4, 5, and 6 seeking to increase the maximum administrative assessment rates of the Appalachian, Southeast, and Florida orders. Specifically, the maximum administrative assessment rates collected on pooled producer milk in the Appalachian, Southeast, and Florida orders will be increased from the current maximum administrative assessment rate of \$0.05 per cwt to \$0.08 per cwt. Proposal 4 was submitted by the Appalachian Market Administrator and Proposals 5 and 6 were submitted by the Market Administrator for the Southeast and Florida orders. These proposals were addressed in a separate recommended decision that solicited comments and exceptions to the proposed assessment rate increase. No comments or exceptions to the recommended decision were received.

1. Class I Prices – Adjustments and Pricing Surface

A witness appearing on behalf of the proponents, Dairy Cooperative Marketing Association (DCMA) testified in support of temporarily increasing minimum Class I prices in the three southeastern milk marketing orders. The witness testified that all elements of their proposals are offered as a “single package” to address the needs of all the southeastern region’s dairy industry stakeholders. It was the opinion of the witness that the supply of milk for fluid use in these marketing areas is threatened and that several simultaneous changes to the provisions of the three orders are needed to attract a sufficient quantity of milk to meet the fluid needs of the markets.

According to the witness, DCMA consists of nine Capper-Volstead cooperative members that include Arkansas Dairy Cooperative Association, Damascus, AR; Cooperative Milk Producers Association, Inc., Blackstone, VA; Dairy Farmers of America (DFA), Kansas City, MO; Dairymen's Marketing Cooperative, Inc., Mt. Grove, MO; Lone Star Milk Producers, Inc., Windthorst, TX; Maryland & Virginia Milk Producers Cooperative Association, Inc. (MD-VA), Reston, VA; Select Milk Producers, Inc., Artesia, NM; Southeast Milk, Inc. (SMI), Belleview, FL; and Zia Milk Producers, Inc., Roswell, NM. The witness testified that each of the DCMA members marketed and pooled milk in one or more of the three southeastern milk marketing order areas during 2006.

According to the DCMA witness, during December 2006 members of DCMA pooled more than 87 percent of cooperative and non-member producer milk on the Appalachian order, more than 87 percent of the cooperative and non-member producer milk on the Southeast order, and more than 96 percent of the cooperative and non-member producer milk on the Florida order.

The DCMA witness testified that their proposed changes to the Class I pricing surface better reflect the actual cost of transporting milk and the pattern in which milk produced outside of the marketing areas moves into the three marketing areas. According to the witness, the cost of procuring milk for fluid use for the southeast region has increased because local production is in serious decline and continues to decline at an increasing rate. The witness noted that the three southeastern orders collectively import more than one-third of the region's milk supply during the most deficit months of the year to cover the fluid milk needs. Fluid demand exceeds 300 million pounds of milk each month in

the three southeastern marketing areas, the witness said. The witness characterized the economic situation of the dairy industry in the region as dire and marketing conditions as disorderly. The witness asserted that producers currently experience inequitable prices for their milk, that handlers have unequal costs, and that there are insufficient economic incentives for the procurement of milk supplies.

The DCMA witness characterized the southeastern region as having rapid population growth. The witness indicated that the U.S. Census Bureau population growth estimates for the states of Alabama, Arkansas, Florida, Georgia, Mississippi, Louisiana, North Carolina, South Carolina, and Tennessee have collectively increased by 8.4 percent from 2000 to 2006, while the population of the U.S. as a whole increased 6.2 percent.

Using market administrator statistics on in-area milk production for the three southeastern marketing order areas, the DCMA witness contrasted population growth to the region's milk production to demonstrate that the dairy industry is in serious decline. The witness said that during 2006 milk was delivered into the three southeastern orders from at least 27 States. The witness explained that local in-area milk production (milk produced within the geographic marketing area boundaries) during 2006 for both the Appalachian and Southeast areas supplied the entire Class I needs of these two areas only 4 months of the year and Florida's in-state milk production was insufficient to supply the Class I needs in every month of 2006. The witness estimated that the Appalachian and Southeast marketing areas are able to supply only about 76 percent of the milk necessary to meet Class I, Class II, and reserve demands, while in Florida in-area producers are able to supply only about 66 percent of the milk necessary to meet Class I and reserve demands annually. The DCMA witness asserted that minimum Federal order Class I

prices have increased only twice in the past 22 years — as a part of the 1985 Farm Bill and as part of Federal milk order reform made effective in January 2000. Specifically, the witness related that the Class I differential for Atlanta increased from \$2.30 to \$3.08 per cwt in 1985 but was increased by only \$.02 to \$3.10 in January 2000. According to the witness, under Federal order reform, some Class I differentials in distant milk surplus areas were increased more than in the milk-deficit regions of the southeast.

The DCMA witness was also of the opinion that changes to the Class I price surface resulted in a flattened price surface and narrowed producer blend price differences between orders. The witness testified that such changes diminished the economic incentives to move milk within the southeastern marketing areas as well as to move milk into the deficit southeastern region of the U.S. According to the witness, minimum Class I price differences and returns to producers are simply not high enough to move milk into these deficit markets without substantial over-order premiums.

The DCMA witness explained that since 1986 diesel fuel prices have risen more rapidly than Class I differentials (and thus Class I prices) in the southeastern region. Relying on data of the Energy Information Administration (EIA) of the U.S. Department of Energy, the witness noted that the U.S. average diesel fuel price increased by 187 percent from 1986 and 2006 (from \$0.94 per gallon to \$2.07 per gallon.) The witness compared this increase to the 0.64 percent or \$0.02 per cwt increase in the Class I differential for Atlanta since 1986.

The DCMA witness testified that the slope of the Class I pricing surface should be changed to progressively increase Class I prices as milk moves to the east and south within the three marketing areas. The witness was of the opinion that changing the slope

of the Class I price surface inside the three marketing areas in this way would better encourage milk to move within the marketing areas. Additionally, the witness was of the opinion that pricing signals to producers would direct their supplies to the most milk-deficit portions of the region. In this regard, the witness added that simply raising Class I prices uniformly throughout the three marketing areas would not result in improved pricing signals to producers.

The DCMA witness explained that in developing the proposed Class I price structure and adjustments to current Class I price levels, DCMA considered two alternatives. According to the witness, in one pricing alternative all the Class I price relationships between plants in the three southeastern orders could be retained. However, under this alternative, the witness explained, the Class I prices for the plants on the outer edges of the Appalachian and Southeast marketing area boundaries would increase considerably, resulting in significant changes in price relationships between those plants and plants regulated by adjoining Federal orders.

Alternatively, the DCMA witness said that the slope of the Class I price surface within the three marketing areas could be altered to minimize plant-to-plant Class I price relationship changes. The witness testified that this approach would result in a pricing structure that better reflected actual milk movements from within and outside of the marketing areas. The witness pointed out that in either approach, plant-to-plant price relationships would change and that the method they chose provided the least change in plant-to-plant price relationships.

The DCMA witness also stressed the need for the proposed Class I price adjustments to remain aligned with the Class I price structure in adjoining marketing areas. The

witness said that the proposed Class I price surface outside of the three southeastern marketing areas would not be changed. The witness was of the opinion that the proposed Class I price adjustments are reasonably aligned with Class I prices in adjoining marketing areas. Through an analysis of plant-to-plant movements of packaged milk, the witness indicated that DCMA's proposed Class I pricing structure provides pricing adjustments that are reasonable and improves the slope of the Class I price surface.

The DCMA witness explained that both a most distant demand point and several supply locations were identified in developing the proposed Class I price surface. The witness indicated that Miami, FL, was identified as the most distant demand point in the southeastern region from any alternative milk supply area. According to the witness, the five possible major supply locations and their distance to Miami were also identified. These locations included: Wayne County, OH; Jasper County, IN; Hopkins County, TX; Lancaster County, PA; and Franklin County, PA.

The witness indicated that of the five possible supply sources, Wayne County, OH, was determined as the least cost supply location with a calculated Class I price adjustment of \$6.14 per cwt at Miami, FL. The witness testified that Class I price adjustments were progressively adjusted to smaller and smaller values as plant location values in the southeastern region were adjusted by their distance from the supply locations.

According to the DCMA witness, the plant-to-plant cost of moving packaged milk was analyzed. The witness testified that successive movements of packaged fluid milk from the outer edge of the Appalachian and Southeast marketing areas towards Miami, FL, were analyzed. As with bulk milk movements, the witness explained, at each plant

location the minimum cost of moving packaged milk was determined and compared to the minimum costs of moving bulk milk. The witness concluded that the bulk and plant-to-plant packaged milk movements were very similar.

The DCMA witness testified that the calculated Class I pricing adjustments were re-adjusted so that plants located near each other would have a similar Class I price adjustment. The witness also acknowledged that the proposed pricing structure could not maintain current Class I price relationships because the current Class I price surface does not reflect actual hauling costs. According to the witness, the west-to-east proposed increase in Class I price adjustments reflects higher hauling costs.

The DCMA witness characterized the proposed adjustments to the calculated Class I price surface as being the result of “smoothing.” The witness explained that deviation from the calculated Class I price adjustment represents the incorporation of best professional judgment in assuring that plants located near each other have the same Class I price adjustment and the need to maintain alignment with Class I prices in adjoining marketing areas.

According to the DCMA witness, the proposed adjustments for plant locations regulated by the Appalachian order would increase in the range of \$0.10 per cwt to \$1.00 per cwt; plants regulated by the Southeast order would increase in the range of \$0.10 per cwt to \$1.15 per cwt; and plants regulated by the Florida order would increase between \$1.30 per cwt to \$1.70 per cwt. Relying on market administrator data, the DCMA witness concluded that the proposed Class I price increases would generate higher marketwide pool values in all three southeastern orders. According to the witness, the estimated annual increase of the Appalachian order pool for 2004, 2005, and 2006 resulting from

the proposed Class I prices alone would have totaled \$19.3 million, \$18.6 million, and \$18.3 million, respectively. For the Southeast order, the witness said, the annual pool value increase would have totaled \$16.8 million, \$17.1 million, and \$17.7 million, respectively. For the Florida order, the witness said, the annual increase in pool value would have totaled \$36.4 million, \$38.3 million, and \$39.2 million, respectively. In estimating the impact on minimum prices paid to dairy farmers, the witness said that average annual minimum uniform prices (as announced at current locations) would have increased by approximately \$0.25 per cwt to \$0.26 per cwt for the Appalachian order, approximately \$0.64 per cwt higher for the Southeast order, and \$1.19 per cwt to \$1.22 per cwt higher for the Florida order.

The DCMA witness acknowledged and explained that changes in Class I price relationships between plant locations resulting from any changed Class I price surface would be inevitable. In this regard, the witness asserted that the price adjustment differences between plant locations under the DCMA proposal would not exceed the cost of moving Class I fluid milk products and therefore would not result in the uneconomic movement of milk.

The DCMA witness concluded by testifying that orderly marketing would be improved with a Class I price structure that is more reflective of the true hauling costs to supply the milk-deficit southeastern region. The witness urged that the proposed Class I price adjustments and pricing surface be adopted immediately. The witness reiterated that the proposed Class I price adjustments be temporarily adopted pending any system-wide changes to the Class I differential level and pricing surface.

A total of 11 dairy farmers whose milk is pooled on at least 1 of the 3 southeastern orders testified at the hearing in support of DCMA's package of proposals, but suggested modifications on how the package should be changed.

Three of the dairy farmers who testified were cooperative members of MD-VA, DFA, and SMI (cooperatives previously described as member organizations of DCMA). These witnesses testified that the dairy industry in the southeastern region is in need of changes to the three marketing orders to respond to the decline in regional milk production. Their testimonies joined that of the DCMA witness supporting the DCMA proposals.

A dairy farmer whose milk is marketed on the Southeast and Florida marketing orders testified on behalf of Cobblestone Milk Producers, Inc. and Mountain View Farms of Virginia in limited support of the Class I price surface feature of DCMA's package of proposals provided certain modifications were made. This witness agreed with proponents concerning the decline of milk production in the southeastern region and the need to import supplemental milk supplies. According to the witness, lower producer pay prices in the southeastern region have led to rapidly declining production that is not being replaced by new farms or the expansion of existing farms. It was the opinion of this witness that the projected increases in producer pay prices arising from the proposed increase in Class I prices would not be enough to affect production trends in the southeastern region. The witness expressed concern that Class I processors would demand their over-order premiums be lowered to compensate for increases in the three orders' minimum Class I prices. The witness requested that the proposed Class I price adjustments for the Appalachian and Southeast marketing areas be increased but did not offer specific amounts.

Four dairy farmers from North Carolina testified in general support of the proposed Class I price adjustments. Three of the witnesses represented organizations that were part of the Southeast Producers Steering Committee (SPSC), whose members include North Carolina Dairy Producers Association, Georgia Milk Producers Association, Upper South Milk Producers Association, Kentucky Dairy Development Council (KDDC), North Carolina Department of Agriculture and Consumer Services, and the North Carolina Farm Bureau Federation. All four witnesses were of the opinion that the proposed Class I price adjustments would not be adequate to increase prices paid to dairy farmers in order to stem the decline of milk production in the southeastern region. The witnesses were of the opinion that additional efforts should be made to enhance local milk production. One dairy farmer witness testifying on behalf of the KDDC said that other adjustments needed to be made to the proposed Class I price adjustments because Kentucky dairy farmers would benefit less from the proposed adjustments than dairy farmers located in the Southeast and Florida marketing areas. Another North Carolina dairy farmer witness offered the opinion that Appalachian producers would need to receive at least a \$1.00 to \$1.50 per cwt increase in their mailbox price to stimulate local milk production. A third North Carolina dairy farmer witness stressed that more emphasis should be made on increasing local milk production rather than seeking better ways to import milk into the region. Another dairy farmer, also from North Carolina, expressed concern that over-order premiums might fall because of the proposed Class I prices adjustments. In addition, an SPSC witness, as well as others, called for a comprehensive study to identify problems and alternatives to the proposals regarding the decline of milk production in the southeastern region.

A witness appearing on behalf of National Dairy Holdings (NDH) testified in limited opposition to the Class I price adjustments of the DCMA package. According to the witness, NDH is a national dairy processor with facilities located throughout the United States. The witness indicated no specific opposition to Class I price increases but conditioned such increases on the fair distribution of the revenue to producers in the southeastern region. While the witness testified that NDH has no difficulty procuring milk for its plants located in the southeastern region, the witness acknowledged other testimony that identified milk production problems of the southeastern region and that the region's producers are in need of relief. The witness expressed concern on how the proposals would impact NDH's wholesale packaged milk sales. The witness also suggested that issues discussed at the hearing could be addressed by utilizing a point-of-sale or plant-point pricing method.

A witness appearing on behalf of the Kroger Company (Kroger) testified in opposition to the proposed Class I price adjustments for the Appalachian and Southeast marketing orders. According to the witness, Kroger operates four fluid distributing plants regulated by the Appalachian and Southeast orders (Winchester Farms, Westover Dairy, Heritage Farms Dairy, and Centennial Farms Dairy). The opinion of the witness was that the proposed Class I price adjustments would disrupt traditional pricing relationships, which were established by the 1985 Farm Bill, and would generate competitive discrepancies with adjoining markets.

The Kroger witness testified that the proposed Class I price adjustments would place their plants in an unacceptable competitive situation with each other in the Appalachian and Southeast marketing areas. Specifically, the witness requested that the Class I price

adjustments for Louisville, KY; Lynchburg, VA; Murfreesboro, TN; and Atlanta, GA be unchanged. The witness also suggested that Winchester, KY, be increased by no more than \$0.10 per cwt in order to maintain competitive milk procurement price relationships with other plants located in the Cincinnati area of the Midwest milk marketing area. The witness opposed the proponent's position that the proposal be considered on an emergency basis.

A witness appearing on behalf of the Milk Industry Foundation (MIF) testified in opposition to the Class I price adjustments of DCMA's package of proposals. According to the witness, MIF is a member organization of the International Dairy Foods Association (IDFA) which represents 115 member companies that market approximately 85 percent of the nation's milk and dairy products. The witness testified that the proposed changes are not necessary because an adequate supply of milk already exists for the Appalachian, Southeast, and Florida orders. The witness stated that because the Federal order system is a national market, milk is available from anywhere in the country. The witness noted over-order premiums compensate those entities who supply the deficit regions. The witness was of the opinion that declining milk production in the southeastern region has been occurring for many years and as such does not warrant an increase in Class I prices. Accordingly, the witness said, emergency action is not warranted.

The MIF witness was of the opinion that Class I prices cannot be changed in one region of the country without affecting milk marketings in other regions. The witness said that the proposed Class I price adjustments would change the competitive relationships between plants located within and outside of the three southeastern

marketing areas. The witness argued that Class I sales would be discouraged because all Class I plants in the three marketing areas would be required to pay a higher price for milk. The witness requested a comprehensive analysis of the national market before adopting the proposed Class I price adjustments.

A witness appearing on behalf of Dean Foods Inc. (Dean) testified in opposition to the proposed Class I price adjustments of DCMA's package of proposals. The witness agreed with testimony of other witnesses indicating the deficit milk supply conditions in the three southeastern marketing areas and the need to increase prices paid to the region's local dairy farmers.

The Dean witness was of the opinion that a comprehensive analysis of the potential impacts of changing the Class I price surface in the three marketing areas had not been conducted. The witness characterized DCMA's package of proposals as containing "too many moving parts" that make it difficult to evaluate the impact of the proposed Class I price adjustment features. The witness was of the opinion that Appalachian and Southeast marketing area dairy farmers are in greater need of higher producer prices than dairy farmers in the Florida marketing area and noted that the proposed Class I price adjustments would benefit Appalachian and Southeast marketing area producers the least. In this regard, the witness worried that the prices received by dairy farmers across the southeastern region would be unfairly distributed if the proposed Class I price changes were adopted.

The Dean witness was of the opinion that the proposed Class I price surface and Class I pricing adjustments would change how milk moves to and between plants located within and outside of the three marketing areas. The Dean witness testified that the

assumptions used by DCMA in laying the foundation for the proposed Class I price adjustments and Class I pricing structure are flawed. In this regard, the witness noted that the USDA 1999 Final Decision on Federal milk order reform indicated that the cost of hauling raw milk was linear [cost increases as the distance milk is transported increases at a constant rate], but that the cost of hauling packaged milk was nonlinear. Accordingly, the Dean witness argued that the proposed Class I pricing changes could give distributing plants located outside the marketing areas incentive to change their route dispositions in order to become regulated on one of the three marketing orders.

According to the Dean witness, distributing plants located outside the area could become regulated at the expense of plants located in the area. As a result, the witness concluded, Class I revenue generated by out-of-area distributing plants would be returned to dairy farmers located far outside of the three southeastern marketing areas. The witness offered that perhaps the greatest beneficiaries of the proposed Class I pricing changes could be producers located as far away as Illinois and Indiana.

The Dean witness also criticized reliance on Wooster, OH, (located in Wayne County) as a supply area for the southeastern region and being a basis of DCMA's proposed Class I price adjustments. The witness noted while DCMA identifies Wooster, OH, as a supply area for the southeastern region, a Pennsylvania State proceeding held in 2006 indicated the testimony of a DFA witness saying that milk was not available in the Wooster, OH, area to supply Pennsylvania.

The Dean witness offered nine modifications to DCMA's package of proposals. The witness explained that their proposed modifications to the package of proposals would not seek to provide higher Class I prices or change the Class I pricing surface. According

to the witness, the Appalachian and Southeast marketing orders' pooling provisions should be identical to those of the Florida marketing order (discussed further below).

2. Producer milk – Diversion Limit and Touch-Base Standards

The DCMA witness testified that the diversion limit standards of the Appalachian and Southeast orders should be identical. According to the witness, diversions to nonpool plants allows for the pooling of milk that is transferred from pool to nonpool plants without milk first needing to be delivered to pool plants. In setting a reasonable limit, the witness was of the opinion that diversion limit standards must take into account reserve supplies needed for Class I use, the balancing needs of the markets, and the seasonality of production.

The DCMA witness testified that milk-deficit Federal orders tend to have lower diversion limit standards relative to orders with substantial reserve milk supplies. The witness testified that while the Appalachian and Southeast order diversion limit standards generally reflect their milk-deficit marketing conditions, they are in need of tightening. Specifically, the DCMA witness proposed that the diversion limit standards be 25 percent during each of the months of January, February, and July through November, and 35 percent for each of the months of March through June and for the month of December.

In explaining the analysis conducted in arriving at the proposed new diversion limit standards for the Appalachian and Southeast orders, the DCMA witness testified that daily producer milk receipts by distributing plants regulated by the two orders from January 2004 through December 2006 were compared to the day of the month when daily receipts at distributing plants were the greatest. The witness explained that the differences between the day of the greatest receipts and each day's actual receipts for the

month at distributing plants were then summed. According to the witness, the resulting value represents the amount of additional milk that would need to be pooled as reserve milk to be able to satisfy Class I demands at a distributing plant on the day of their greatest need. The witness stated that the analysis showed that an additional milk volume of 12 to 13 percent of distributing plant receipts would be the minimum reserve necessary to cover daily fluctuations in the demand for fluid milk at distributing plants. On an annual basis, the minimum average reserve needed as calculated is about 22 percent, the witness said.

The witness explained that the proposed diversion limit standards of 25 percent for both orders for each of the months of January, February, and July through November, are based on the analysis described above and the need to provide for an additional reserve in the tightest supply months. The witness explained that the proposed diversion limit standards of 35 percent for each of the months of March through June and the month of December accommodate seasonal fluctuations in supply. The witness explained that this standard would allow regular producers who supply the Class I needs of the marketing areas in the tight supply months to pool all of their additional production in the flush months and accommodate the regular decline in Class I sales that occurs when schools close for the summer months. According to the witness, Class I plants also temporarily close or severely limit their receiving operations over the holiday period in December resulting in substantial surplus milk.

Relying on market administrator data, the DCMA witness estimated that the impact on the minimum uniform prices from lowering the diversion limit standards alone would raise blend prices approximately \$0.02 per cwt and \$0.07 per cwt annually for the

Appalachian and Southeast orders, respectively. The witness indicated that a change in the blend price for any particular producer would vary based on where the producer's milk was delivered.

The DCMA witness stressed that the proposed changes in the two orders' diversion limit standards do not fully capture the true volume of milk likely to no longer be eligible to be pooled on the two orders. The witness explained that if the volume of producer milk delivered to pool plants were the same each month, then the volume of producer milk no longer pooled and priced by the orders would drop about 6.67 percent and 29.72 percent on the Appalachian and Southeast orders, respectively. The witness further explained that lowering the diversion limit standards also should result in increasing minimum order blend prices paid to producers. According to the witness, proposed changes to the diversion limit standards of the orders, together with expected increases in revenue arising from Class I price adjustments and Class I pricing surface, will likely encourage local milk production, the movement of milk into the region from distant sources, or some combination of both.

The DCMA witness testified that the package of proposals also includes the lowering of the touch-base standards of the Appalachian and Southeast orders and makes them identical. According to the witness, this would discourage uneconomic movements of milk and offer operational savings for cooperatives supplying the Class I needs of the marketing area.

The DCMA witness explained that because of the continuing decline in local milk production, an increasing amount of milk that is produced further from the marketing areas is becoming a regular part of the supply of Class I milk. The witness characterized

this milk of distant dairy farmers as the reserve supply needed for balancing the Class I needs of the two marketing areas.

The DCMA witness was of the opinion that reducing the touch-base standard to one day each month in both orders is necessary for the efficient pooling of reserve supplies. The witness testified that lowering the touch-base standard would prevent local milk already supplying the markets' Class I needs from being displaced by milk produced farther from the marketing areas, which is shipped in simply to meet pooling standards. According to the witness, requiring producers to deliver more days to pool plants when the milk is not truly needed results in increasing the cost of supplying the Class I needs of the two markets.

Eight dairy farmers testified in general support of DCMA's proposed changes to the two orders' diversion limit and touch-base standards. Some were of the general opinion that the regular reserve supply for the Appalachian and Southeast marketing areas should be pooled when not delivered to Class I plants. While all supported the pooling of milk that regularly supplies the Class I needs of the two marketing areas, several dairy farmers expressed caution that the diversion limits were not being lowered enough while touch-base standards were needlessly being lowered. According to these witnesses, this would encourage pooling milk not truly supplying the markets and result in lower blend prices paid to local dairy farmers. The dairy farmers testifying supported adopting needed changes on an emergency basis.

A witness representing Dean testified that the proposed changes to the diversion limit and touch-base standards would not be sufficient to deter the uneconomic movement of milk or to enhance producer prices in the Appalachian and Southeast marketing areas.

According to the witness, current diversion limit standards are in excess of the markets' balancing needs and should be lowered immediately.

The Dean witness characterized the Appalachian and Southeast orders as being very similar to the Florida order in terms of milk consumption and production. The witness was of the opinion that the pooling standards of the Florida order work well and pooling milk not consistently serving the market's Class I needs rarely occurs. The witness specifically proposed that diversion limit standards be changed to 15 percent for each of the months of December through February, 20 percent for each of the months of March through June, and 10 percent for each of the months of July through November.

According to the Dean witness, dairy farmers will receive higher blend prices if diversion limits are made even lower than proposed by DCMA. Relying on market administrator data, the witness stated that January 2004 had shown the highest "need" of reserve milk during 2004-2006 for the Southeast order at approximately 22 percent of total milk pooled on the order. The witness contrasted this with October 2004 when the "needed" reserve was approximately 7 percent. In this regard, the witness suggested that diversion limits could be reduced below that proposed by DCMA. According to the witness, if made too low, the market administrator has the authority to change the diversion limit standards if warranted.

The Dean witness opposed DCMA's proposed one day per month touch-base standard if DCMA's proposed diversion limit standards are adopted. The witness was of the opinion that inefficient movements of milk would result if the one day touch-base standard were adopted. However, the witness indicated support for a two-day touch-base

standard provided the diversion limit standards of the Florida order are simultaneously adopted.

The Dean witness explained that when touch-base requirements are low, locally produced milk can be displaced by milk located far from the marketing area because it needs to be transported to the marketing area fewer times to qualify for pooling and receiving a higher blend price. The witness was of the opinion that only milk that is necessary to serve the Class I needs of the market should be delivered to that market. According to the witness, reserve milk supplies located far from the market should not be pooled on the market if they are not delivered to the market.

3. Transportation Credit Provisions

The DCMA witness explained that on September 1, 2006, the Secretary issued a tentative partial decision (71 FR 54118) which amended the transportation credit provisions of the Appalachian and Southeast orders. Specifically, the witness noted that the decision established a fuel cost adjuster to determine a variable mileage rate factor used to compute the payout of transportation credits and higher maximum transportation credit assessments on Class I milk for the Appalachian and Southeast orders. To accompany these adopted changes that were implemented on December 1, 2006, (71 FR 62377) the witness proposed four other changes to the transportation credit provisions that are part of the package of changes proposed for the two southeastern orders.

According to the DCMA witness, the four additional changes to the transportation credit provisions for both orders include: 1) extending the months during which transportation credits may be paid to include the months of January and February with June being an optional transportation credit payment month; 2) expanding the payment of

transportation credits to apply to the full load of milk, rather than the current calculated Class I portion of milk loads; 3) providing greater flexibility for supplemental milk producers to be eligible to receive transportation credit payments; and 4) raising the maximum monthly transportation credit assessment for the Southeast order from the current \$0.20 per cwt to \$0.30 per cwt.

According to the DCMA witness, the need for supplemental milk in the Appalachian and Southeast orders has increased during the months of January and February. The witness offered evidence showing that during January 2004 through December 2006, January and February are months with increasing Class I use in the Appalachian and Southeast orders. The witness claimed that during January and February, local milk is not sufficient to supply the Class I milk needs. It is this combination of Class I need and available local producer supplies that show January and February as being more like the current transportation credit payment months of July through December than the flush months of March through May, the witness concluded. According to the witness, adding January and February as transportation credit payment months would give suppliers of supplemental milk an opportunity to recoup a portion of the hauling costs to supply the marketing areas with milk for fluid use.

In explaining this proposed change, the DCMA witness said, in part, current transportation credit payment provisions result in reimbursements that are much lower than the real cost of hauling. The witness explained that the cost of hauling milk to Class I plants is the same regardless of the plant's use or the Class I utilization of the market. The witness was of the opinion that expanding the transportation credit payments to full loads of milk delivered only to pool distributing plants would enhance orderly marketing

and better ensure that sufficient supplemental milk is delivered to pool distributing plants. The witness supported continuing transportation credit payments on supplemental milk deliveries to pool distributing plants only.

The DCMA witness proposed simplifying the process for determining what supplemental milk is eligible for transportation credit payments. The witness noted that currently, a dairy farm must be located outside either the Appalachian or the Southeast marketing areas, the dairy farmer must not meet the Producer provision under the two orders during more than two of the immediately preceding months of February through May, and not more than 50 percent of the dairy farmer's milk production during those two months, in aggregate, can be received as producer milk under the order during those 2 months.

The DCMA witness was of the opinion that the requirements for transportation credit payment eligibility should be changed to provide flexibility in meeting the criteria while limiting the receipt of transportation credits to only that milk which is truly supplemental and that is not part of the consistent and regular supply of milk serving the Class I needs of the two markets. Specifically, the witness proposed that: 1) a dairy farmer must not meet the Producer definition on the orders in more than 45 of the 92 days in the months March through May, or 2) a dairy farmer must have less than 50 percent of their producer milk pooled on the orders during those 3 months combined. The witness argued that limiting the producer association with the orders to no more than half the time or to no more than half their milk production is sufficient to identify a dairy farmer as a supplemental supplier of milk to the marketing areas. These changes, the witness

asserted, offer substantial cost savings to cooperatives that bear the burden of sourcing and supplying the supplemental milk needs of the markets from distant locations.

The DCMA witness testified that the maximum transportation credit assessment for the Southeast order needs to be increased from the current \$0.20 per cwt to \$0.30 per cwt given the proposed expansion of the transportation credit payments on full loads of milk to Class I distributing plants regulated by the two orders. The witness was of the opinion that otherwise the current assessment rate would be insufficient to cover anticipated shortfalls in the transportation credit balancing fund.

While the DCMA witness proposed a higher transportation credit assessment rate for the Southeast order only, the witness projected that the proposed changes to Class I prices and the Class I pricing surface in the Appalachian and Southeast orders would lessen payments from the transportation credit balancing funds. The witness explained this may occur because of the greater positive differences (increases) from adopting the proposed Class I price adjustments and Class I pricing surface. The witness did acknowledge that the additions of the months of January and February as transportation credit payment months would tend to increase transportation credit payouts.

Relying on market administrator data, the DCMA witness estimated that for the months of July through December 2006 the Southeast order transportation credit payments would total \$15,704,872 as a result of their proposal, and January and February 2006 payments would total approximately \$2,900,000, resulting in an overall amount of approximately \$18,604,872. At the current assessment rate of \$0.20 per cwt, the witness concluded that transportation credit balancing funds would not have been sufficient to pay all transportation credit claims in 2006. At the proposed \$0.30 per cwt assessment

rate, the witness was of the opinion that sufficient revenue would be generated to satisfy all transportation credit claims.

Relying on market administrator data for the Appalachian order, the witness said that during July 2006 through January 2007, transportation credit payments would have totaled approximately \$4,073,312. According to the witness, February 2006 would have included a payment of approximately \$313,000, bringing the total estimated transportation credit payments to \$4,383,312. According to the witness, the current \$0.15 per cwt assessment rate for the Appalachian order would have been sufficient and no increase in the assessment rate would be needed.

The DCMA witness supported continuing to provide for market administrator discretion in setting the transportation credit assessment rates at less than the maximum allowed. The witness was of the opinion that doing so will prevent the needless collection of revenue when the transportation credit balancing funds are sufficient to meet claims.

Four dairy farmers testified in support of DCMA's proposal to provide additional flexibility in determining which producers are supplying supplemental milk to the two marketing areas. As with other features of DCMA's proposals, these dairy farmers supported adoption of these proposed changes on an emergency basis.

The witness appearing on behalf of Dean expressed support for adding the months of January and February as transportation credit payment months for the Appalachian and Southeast orders on the condition that tighter diversion limits be adopted. The witness said these months should be considered as payment-eligible months because the tentative decision implemented in December 2006 eliminated the ability to divert milk on loads of

milk seeking the payment of a transportation credit. However, the Dean witness opposed expanding transportation credit payment eligibility to entire loads of milk. In this regard, the witness expressed concern that this would essentially result in Class I sales funding the supply of supplemental milk in lower-valued Class II uses.

4. Administrative Assessment Rate

According to the Assistant Market Administrator for the Appalachian order, Proposal 4 was offered to ensure that sufficient funds are available for administering the Appalachian order. The witness added that Proposal 4 would amend section 1005.85 (7 CFR 1005.85) to provide for all of the administrative assessment language pertinent to the Appalachian order provisions and would discontinue the reference to section 1000.85 (7 CFR 1000.85). The witness explained that administration and operating costs include administrative, accounting, human resources, economic, pooling and audit staff expenses.

The Assistant Market Administrator for the Appalachian order stated that the market administrator is required to maintain a specific level of operating reserves. The reserve level, the witness said, must be maintained in the event that an order is terminated and would fund the necessary costs for closing out an order, completing pools and audits and paying severance and leases. The reserve level is detailed in the MA Instruction 207 that is issued by the Dairy Programs Deputy Administrator, said the witness.

The Assistant Market Administrator for the Appalachian order said that the majority of the administrative assessment revenue comes from pooled producer milk. Additionally, the witness said, assessments are also collected on other source receipts assigned to Class I and certain route disposition in the marketing area by partially regulated distributing plants. The witness stated that although the maximum

administrative assessment rate allowable on pooled producer milk is \$0.05 per cwt, the rate currently collected each month is \$0.04 per cwt, which has remained unchanged since January 2000.

The Assistant Market Administrator for the Appalachian order said that during 2000-2002, producer milk pooled on the Appalachian order averaged 547 million pounds per month. According to the witness, the \$0.04 per cwt assessment rate at this volume of milk created enough revenue to fund Appalachian order operations and maintain the mandated operating reserve. The witness stated that from 2003-2005, producer milk pooled on the order averaged 525 million pounds per month and in 2006, producer milk pooled on the order averaged 520 million pounds per month. The witness also compared the first 4 months of 2007 to the first 4 months of 2006 and stated that producer milk pooled on the order was down 3.45 percent.

The Assistant Market Administrator for the Appalachian order explained that about \$215,000 is needed each month to cover basic operating expenses. By keeping the assessment rate of \$.04 per cwt, the witness said 538 million pounds of producer milk would be needed each month to cover monthly order expenses. The witness further explained that the Appalachian order was in an operating deficit in 2003, 2004, and 2006 and had a balanced budget in 2005. During 2003-2006, the witness said, the volumes of pooled producer milk did not generate sufficient revenue to fund order operations and lowered the mandated operating reserves.

According to the Assistant Market Administrator for the Appalachian order, a decision effective December 1, 2006 (71 FR 62377), established a zero diversion limit standard on Class I milk receiving transportation credits. The decision, the witness said,

reduced the amount of milk that could be pooled on the order and reduced the amount of assessment revenue collected during the period of July through December, when those volumes of milk would be pooled. In addition, the witness said that Proposal 1, if adopted, would add January and February as additional transportation credit payout months, further reducing the amount of milk that could be pooled on the Appalachian order. The witness stressed that tightening pooling provisions of the order impacts the amount of producer milk pooled on the order. The witness expressed concern that less milk pooled on the order would reduce administrative assessment revenue and the ability to fund order operations while maintaining the mandated reserve level.

The Assistant Market Administrator for the Appalachian order said that the market administrator makes efforts to control costs of carrying out order operations. According to the witness, cost control efforts include a reduction of office staff by 29 percent through attrition since January 2003, contracting with outside computer services, negotiating a telecommunications contract, consolidating a field office, and reducing travel and mail expenses. The witness stressed that regardless of the market administrator's efforts to control costs and efficiently administer the order, gains in efficiency cannot make up for revenue lost due to a reduction in milk volumes.

The Assistant Market Administrator for the Appalachian order concluded by emphasizing that increasing the maximum administrative assessment rate to \$.08 per cwt would be the maximum rate allowable and not necessarily the rate assessed. The witness said the actual rate assessed would only be as high as determined by the market administrator with approval by the Dairy Programs Deputy Administrator.

According to the Market Administrator for the Southeast and Florida orders, Proposals 5 and 6 were offered to ensure that there are sufficient funds to carry out administration of the orders. The witness said the proposals would amend sections 1006.85 (7 CFR 1006.85) and 1007.85 (7 CFR 1007.85) to provide for all of the administrative assessment language pertinent to the Southeast and Florida orders, and would discontinue the reference to section 1000.85 (7 CFR 1000.85). The witness explained that administration and operating expenses of the order include pooling, auditing, and providing market information.

The Market Administrator for the Southeast and Florida orders explained that the order is required to maintain a specified level of operating reserves. The reserve level, the witness said, is detailed in the MA Instruction 207 that is issued by the Dairy Programs Deputy Administrator. The witness said the reserve level is kept to cover necessary costs of closing out an order, such as completing pools, audits, and paying severance and lease payments.

The Market Administrator for the Southeast and Florida orders explained that the majority of the monthly administrative assessment is collected from pooled producer milk. The witness added that additional assessments are also collected from other source receipts associated with Class I and certain route disposition in the marketing area by partially regulated distributing plants. The witness stated that the market administrator largely depends on the administrative assessment revenue to fund the operations of the orders. The witness noted that since 2000, the administrative assessments for both the Southeast and Florida orders have contributed over 80 percent of the total income of the market administrator office.

According to the Market Administrator for the Southeast and Florida orders, the combined monthly average of pooled producer milk for the two orders in 2000 was 862.8 million pounds. In 2001, the witness said, the combined monthly average of producer milk pooled in both orders was 878.4 million pounds and in 2002, the combined monthly average was 885.0 million pounds. The witness said that during 2000-2002, the assessment rates charged in the Southeast and Florida orders of \$0.035 and \$0.03 per cwt, respectively, along with the volume of producer milk, were sufficient to fund order operations and maintain the mandated reserve funds.

The Market Administrator for the Southeast and Florida orders said that in 2003, although producer milk in the Florida order increased by 5 percent, producer milk in the Southeast order decreased 11 percent, resulting in a considerable decrease in assessment collections. According to the witness, during 2003, funds were drawn from the operating reserves, reducing the reserve level near the mandated minimum. The witness said that as a result, effective with January 2004 milk deliveries, the administrative assessment rates increased by \$0.01 to \$0.045 and \$0.04 per cwt for the Southeast and Florida orders, respectively.

The Market Administrator for the Southeast and Florida orders stated that in 2004, the monthly average pounds of producer milk pooled increased over 2003 by 1 percent and 5 percent in the Southeast and Florida orders, respectively. The witness added that in 2005, producer milk increased over 2004 by 5 percent and 8.8 percent in the Southeast and Florida orders respectively, and in 2006, producer milk increased over 2005 by 6.8 percent and stayed the same in the Southeast and Florida orders, respectively.

According to the Market Administrator for the Southeast and Florida orders, the administrative assessments implemented in 2004, with the increase in producer milk during 2004-2006 and efforts to control costs, have been sufficient to cover operating expenses and build an adequate reserve level. The witness added that they continue to take measures to control costs. The witness said that from 2000-2006, cost control measures included a 15 percent reduction in staff through attrition, increased use of technology to hold meetings and conduct audits, a reduction in travel expenses, and a decrease in communication costs.

The Market Administrator for the Southeast and Florida orders explained that Proposal 2 seeks to limit an average of 12.3 percent of allowable diversions in the Southeast order which would reduce the amount of milk pooled on the order, as well as the value of administrative assessments used to fund order operations. The witness also noted a decision effective December 1, 2006, (71 FR 62337) that reduced allowable diversions by the volume of transportation credit claims. The witness also expressed concern that the downward trend in Southeast milk production and marketing decisions made by handlers provides an increased potential for variability in the revenue available for order operations.

The Market Administrator for the Southeast and Florida orders concluded that while the proposals seek to increase the maximum assessment rate from \$0.05 per cwt to \$0.08 per cwt, the \$0.08 per cwt would not necessarily be the rate charged. The witness stressed that the assessed rate would only be high enough to cover operating expenses and maintain the mandated reserve level as approved by the Deputy Administrator for Dairy Programs.

Post-Hearing Briefs

Post-hearing briefs were filed by: Dairy Cooperative Marketing Association (DCMA), Southeast Producers Steering Committee (SPSC), Dean Foods Company and National Dairy Holdings (Dean/NDH), and the Milk Industry Foundation (MIF).

The DCMA post-hearing brief echoed the association's support for adoption of their proposals on an emergency basis. The brief stated that its proposals were developed as an integrated package and that the package of proposals better assures the Appalachian, Southeast, and Florida milk orders' ability to attract a sufficient quantity of milk for fluid use. The brief said this is accomplished by increasing the Class I prices in the three milk marketing orders, lowering the diversion limit and touch-base standards, and modifying the transportation credit provisions. The brief reiterated the deficit milk supply situation in the southeastern region. The brief emphasized that procuring milk for Class I use for the region is a major challenge that is borne disproportionately by cooperative associations and their dairy farmer members.

The DCMA brief explained that the proposed Class I price adjustments and changes to the Class I pricing surface in the Appalachian, Southeast, and Florida orders would accomplish two needed results. According to the brief, the changes would likely encourage local producers to increase milk production and provide pricing incentives for producers located outside the marketing areas to deliver milk to the three marketing areas for fluid use.

The DCMA brief stated that, while plant price relationships would inevitably change as a result of its proposals, the Class I prices proposed are strikingly similar to plant price differences adopted in the 1999 Order Reform final rule. The brief indicated that this is

proof that its method of developing the proposed Class I price adjustments and Class I pricing surface is valid and meets the requirements of a regulated Class I price system.

The DCMA brief commented on the method used in developing its Class I pricing proposals as deviating from a model developed by Cornell University that was relied upon in the adoption of current Class I pricing structure. The brief addressed opponent arguments that the cost of shipping bulk versus packaged milk follows distinct cost equations and, therefore, different cost curves. According to the brief, the marginal costs involved in shipping bulk milk long distances (over 900 miles) are still greater than zero and subsequently do not invalidate their proposed pricing structure. The brief characterized the proposed Class I pricing portion of the proposal package as containing all the elements used by the Department in the current Class I pricing structure. The brief also argued that DCMA's proposals generate Class I pricing relationships consistent with the objectives of marketing orders in assuring an adequate supply of milk for the three marketing areas, not encouraging the uneconomic movement of milk, and being reflective of the supply and demand conditions for milk within the marketing areas.

The DCMA brief explained that lowering the diversion limit standards in the Appalachian and Southeast orders would serve to enhance producer blend prices while the decrease in the producer touch-base standard would act to encourage more efficient milk movements and offer cost savings to milk suppliers. The brief maintained that while some witnesses testified in support of even lower (tighter) diversion limits, no evidence to support such changes was presented. The brief added that diversion limit standards in both orders will effectively be much lower than the proposed standards because no diversions may accompany supplemental milk pooled on the order which

receives a transportation credit payment. The brief also noted that DCMA's proposal for extending transportation credit pay-out months also effectively lowers pooling milk by diversion.

The DCMA brief stated that extending the payment of transportation credits to include the months of January and February and to the entire loads of milk would offer the suppliers of supplemental milk greater assurance that more of the actual costs of hauling milk to the southeastern region would be covered. According to the brief, simplifying the criteria that determines if producers are supplemental suppliers of milk to the marketing areas offers both administrative and marketing efficiencies. Finally, the brief explained that the proposed increase in the transportation credit assessment for the Southeast milk order will ensure that transportation credit payment claims are adequate to meet anticipated needs.

The DCMA brief maintained that the record contains abundant evidence supporting the existence of emergency conditions in the three marketing areas affecting the ability to adequately supply fluid milk. The brief stressed that providing adjustments for higher Class I prices and modifying the Class I pricing surface, if even on a temporary basis, is necessary immediately. The brief indicated that milk production in the Southeastern states during the first quarter of 2007 declined at a faster rate than the annual decline during 2006 and 2005, and that this increasing rate of milk production decline cannot be ignored. The brief reiterated the continuing increases in hauling costs and the longer distances milk must be shipped to provide sufficient supplies to meet fluid demands.

A post-hearing brief was submitted on behalf of SPSC. The SPSC brief indicated support for the Class I portions of DCMA's proposals but was not fully supportive of the

proposed diversion limit standards, touch-base standards, and transportation credit provisions. The brief agreed with the DCMA proposals to increase Class I prices in the Appalachian, Southeast, and Florida orders on an emergency basis because it would promote milk production within the three marketing areas by enhancing local producer income – the primary suppliers of fluid milk for the three southeastern markets. The SPSC brief did express concern that even with expected higher blend prices to producers accruing from higher Class I prices, the current trend of lower local milk production may not be slowed.

The SPSC brief indicated support to lower (tighten) diversion limit standards in the Appalachian and Southeast orders. However, the brief expressed the opinion that diversion limit standards for both orders could and should be reduced more than that proposed by the DCMA. The SPSC brief asserted that record evidence had not determined the appropriate base and reserve milk supply volumes, the proper diversion limit and touch-base standards for the Appalachian and Southeast orders, or who should bear the costs of maintaining reserve milk supplies for the Southeastern region.

The SPSC brief was of the opinion that record evidence also did not clearly indicate that the volume of milk pooled on the orders for other than Class I use actually would be lowered by adopting DCMA's proposed diversion limit and touch-base standards. According to its brief, the majority of the producer milk removed under the DCMA proposals would be unavailable in only a few months of the flush production months for the Appalachian order and in the months of January and February for the Southeast order. The brief expressed concern that milk could actually be added in both orders in the other months due to the decrease in the touch-base standard. The brief maintained that in-area

producers and those who provide the primary supply of milk for fluid use on a regular basis should receive the greatest share of revenue attributable to that service. According to the brief, pooling more milk than needed would only continue to depress the income of Southeastern producers.

The SPSC brief found agreement with Dean's testimony that proposed a more aggressive lowering of diversion limit standards for the Appalachian and Southeast orders. The brief agreed with Dean's position that tighter diversion limits would sharply reduce the volumes of pooled milk in the two orders and the relative impact on producer pay prices would be more substantial. The brief indicated support for continuing to provide discretionary authority for the market administrators to tighten diversion limits and raise touch-base standards if necessary and without the need to resort to the formal rulemaking process.

The SPSC brief indicated conditioned support for DCMA's proposed changes to the transportation credit provisions of the Appalachian and Southeast orders. However, the brief questioned the proper role of transportation credits in both marketing orders. The brief requested the Department consider the proper levels of producer delivery day requirements, diversion limits, and transportation credit provisions to achieve the stated goals of the DCMA package of proposals.

A post-hearing brief submitted on behalf of Dean and NDH (Dean/NDH) agreed that the Southeastern region of the U.S. is a deficit milk production region and that the deficit is growing. The brief said that dairy farmers who regularly and consistently supply milk to fluid milk plants in the southeastern region should be appropriately compensated for their raw milk and receive the blend price of the order they supply. However, the brief

argued that adopting the proposed Class I price adjustments and the Class I price surface proposals is not supported by record evidence or by rule of law and should be denied.

While the Dean/NDH brief expressed agreement that long-term problems exist regarding the viability of the southeastern region dairy industry, it doubted that correcting problems that have prevailed for 25 years could be solved overnight through emergency rulemaking.

According to the Dean/NDH brief, there is no evidence of an emergency that would warrant adopting the Class I price proposals by the omission of a Recommended Decision. To the extent that conditions warrant the need to rely on milk orders to return higher prices to dairy farmers, the brief asserted that an alternative method of returning higher prices can be achieved by simply lowering the orders' diversion limit standards. The Dean/NDH brief noted that Dean and NDH operate several fluid milk processing plants in the Southeastern region and that other processors testifying at the hearing opposed the Class I price adjustments and Class I pricing surface changes. The brief argued that such changes may have unintended consequences which may worsen the situation in the southeastern region. According to the Dean/NDH brief, adopting changes to Class I pricing may create incentives for plants located outside the Appalachian and Southeast marketing areas to direct their fluid milk sales in the marketing areas and become pooled on those orders. The brief argued that while plants may gain in blend price changes by altering where they become pooled, the price surface may not change for their competitors. The brief also asserted that since January 2000, Class I prices were intentionally linked nationwide as part of Federal milk order reform and concluded that any change in Class I differentials or the Class I price surface, even at one price location,

would change the economic incentive nationwide to serve that location. The brief therefore contended that the entire national Class I price surface needs to be evaluated.

According to the Dean/NDH brief, DCMA's Class I price proposals fail to rely on accepted economic models and fail to follow the Department's established policies for making adjustments to the Class I price surface. Specifically, the brief argued that the economic calculations failed to take into consideration "shadow pricing," which the brief characterized as how a market could react to changes such that an additional price change would alter distribution. The brief also argued that the Class I price proposals fail to calculate unique prices for each location by considering relevant reserve supply areas and fail to account for differences in raw milk movements versus packaged milk movements.

According to the Dean/NDH brief, the rationale for setting a target price for Miami, FL, and then backing off that price and "smoothing" the result is arbitrary and capricious. The brief contended that determining Class I prices in this way applied non-uniform methodology and did not meet the standards of the Administrative Procedure Act. In addition, the brief noted that no evidence or economic data backs up the "smoothing" process as described by DCMA testimony.

The Dean/NDH brief asserted that Wooster, OH, should not be identified as a supply area because it has never been relied upon as any kind of basing point for pricing milk and doing so now would be specifically contrary to testimony given at a Pennsylvania State hearing for a recent State of Pennsylvania rulemaking. Accordingly, the brief contended that DCMA's entire Class I pricing proposals should be rejected.

According to the Dean/NDH brief, although the Class I price changes sought are "temporary," competitive impacts of such changes can be long-term and result in

permanent harm to Class I handlers. The brief asserted that any decision should be considered permanent unless it has a specific sunset provision. According to the brief, no specific sunset provision had been proposed or discussed in the hearing record.

The Dean/NDH brief pointed out that, at the time of the hearing, the dairy industry was also experiencing record high Class I prices for milk further demonstrating the lack of need for emergency action. The brief noted that the May 2007 uniform price for Fulton County, GA, was \$18.37 per cwt. According to the brief, this price is \$1.37 per cwt higher than April 2007 and is \$5.83 per cwt, or 45.3 percent, higher than in May 2006. The brief also noted that the Class I price for June 2007 at Fulton County was \$1.92 per cwt higher than May 2007, and the July 2007 price increased by \$3.07 per cwt. The brief indicated that even a proponent witness acknowledged that such higher prices were likely to continue through the fall 2007.

The Dean/NDH brief agreed that diversion limit standards for the Appalachian and Southeast orders should be lowered on an emergency basis and made identical to those of the Florida order. The brief indicated that the Florida order currently functions well by having lower diversion limit standards and this has supported the prevailing over-order premiums. The brief opined that because of the order's tight pooling provisions, the need for transportation credits and the need for holding numerous formal rulemaking hearings has been avoided. According to the brief, the Florida order's tight diversion limit standards have continually assisted that order in retaining strong blend prices paid to dairy farmers and attracting sufficient amounts of milk supplies.

The Dean/NDH brief asserted that pool revenues should be shared only among those producers who truly and regularly serve the Class I market and that diversion limit

standards of the Appalachian and Southeast orders are not adequately identifying those true and regular suppliers. The brief asserted that both orders can be made more effective by requiring a genuine association of a milk supply with the market as intended by the AMAA.

The Dean/NDH brief indicated that if Dean's proposal for adopting the diversion limit standards of the Florida order for the Appalachian and Southeast orders is adopted, Dean would support the DCMA's one-day per month touch-base standard proposals. As Dean/NDH does not consider DCMA's proposed diversion limit standards as being any change at all, it opposed any change to the touch-base standards of the Appalachian and Southeast orders.

The Dean/NDH brief opposed the expansion of the payment of transportation credits to include the entire load of milk and stated that payments should only be paid on Class I milk as currently provided under the Appalachian and Southeast orders. The brief expressed concern that adopting the proposed changes would create the wrong economic incentives. The brief noted that suppliers of milk to a Class I plant with a higher than market average of Class II use would be receiving a larger economic benefit than Class I plants with below market average Class II use. According to the brief, this would be contrary to assuring equal minimum milk prices among similar handlers.

The Dean/NDH brief was of the opinion that transportation credits have been a key factor in contributing to the decline of the dairy industry in the southeastern region. In this regard, the brief noted the proponents acknowledgement that in some cases current touch-base provisions in conjunction with transportation credits cause inefficient

movements of milk. The brief asserted that transportation credits, not touch-base standards, give rise to inefficient movements of milk.

A post-hearing brief by MIF reiterated its opposition to adopting DCMA's proposals and asserted the absence of emergency marketing conditions that warrant emergency action. The brief noted awareness of declining milk production in the southeastern region but indicated this is not a sufficient basis for the adoption of the proposals on an emergency basis. The brief further argued that no emergency exists to warrant adoption of the proposals because the trends of declining milk production in the region and rising fuel costs have existed for many years.

The MIF brief stressed that the key purpose of the Federal milk marketing order program is to ensure an adequate supply of milk for Class I needs. In this regard, the brief noted that no witnesses testified on the inability to procure milk for Class I use. The brief reiterated that in a survey of its membership conducted before the hearing, no member indicated difficulty securing milk for Class I needs in the three southeastern marketing areas. The brief also mentioned that over-order premiums are paid by Class I handlers to secure milk for fluid use and the proponents testified that current over-over premiums currently offset higher fuel costs.

The MIF brief noted that some southeastern dairy producers who testified at the hearing also participated in a herd-removal program called Cooperatives Working Together (CWT). In this regard, the brief cited this as an example of misplaced concern for declining milk production in the southeastern region.

The MIF brief asserted Class I sales would suffer if higher Class I prices were adopted because higher raw milk costs would increase wholesale costs and result in

higher retail prices paid by consumers. The brief noted that the current, general structure of Class I location differentials has been in place for 22 years and that milk bottlers have made significant investments in plants and equipment during this time.

According to the MIF brief, plants could be disadvantaged in the marketplace solely because of increases in the Class I price relative to the Class I price of its competitors. The brief argued that a \$0.005 difference per gallon could result in lost customers for a distributing plant and that a \$0.025 increase is enough to lose a supermarket account. The brief asserted that increasing a Class I price by \$0.10 per cwt (\$0.0086 per gallon) could yield dire results for a Class I plant. The brief indicated that an unexpected consequence could be that plants distant to the three orders could become associated with one of the three orders due to differences between transportation costs and increased Class I prices resulting in out-of-area plants taking away sales from in-area plants.

The MIF brief said that a comprehensive study and analysis on a national scale of all potential consequences and on demand for packaged milk was needed before any changes to Class I pricing were adopted. The brief reasserted the opinion that Class I prices could not be changed in the southeastern region alone because that would change marketing conditions in all marketing areas.

A post-hearing brief submitted on behalf of DCMA expressed support for the market administrator assessment increase for the Appalachian, Southeast, and Florida milk orders in Proposals 4, 5, and 6, respectively.

Comments and Exceptions

Comments and exceptions to the tentative partial decision (73 FR 11194) were filed by Dairy Cooperative Marketing Association, Inc. (DCMA), Arkansas Milk Stabilization

Board (AMSB), Southeast Producers Steering Committee (SPSC), Dean Foods Company and National Dairy Holdings (Dean/NDH), and the Milk Industry Foundation (MIF).

In comments and exceptions regarding the adopted Class I price surface, DCMA wrote that the amended Class I differentials will send appropriate signals to maintain and increase milk production within the three marketing areas, as well as create incentives to increase the movement of supplemental milk to these areas when needed. DCMA also expressed agreement that the Class I price surface changes will generate producer price increases in all three marketing areas. DCMA reiterated that the reduction in the volume of diverted milk in the Appalachian and Southeast marketing areas should also lead to increased uniform prices in those marketing areas. DCMA predicted that decreases in the touch-base standard will offer greater flexibility in moving pooled milk and will offer cost savings on pooled reserve supplies. Lastly, DCMA supported USDA's decision to maintain and update the transportation credit balancing fund provisions.

Comments and exceptions filed on behalf of the AMSB expressed support for the tentative partial decision, but proposed additional changes to Class I price adjustments for certain county locations in Arkansas. AMSB requested that the Class I differentials for Pulaski county be increased from \$2.80 to \$3.20 per cwt, Sebastian county from \$2.80 to \$3.10 per cwt, and Washington and Benton counties from \$2.60 to \$3.00 per cwt. AMSB also proposed that the touch-base standard be changed from 2 days for each of the months of July through December and to 6 days for each of the months of January through June. According to AMSB, significant decreases in milk production in Arkansas, as well as in Mississippi and Louisiana, are due, in part, to the Federal milk

marketing orders. AMSB was of the opinion that their proposed changes are needed to stabilize dairy production in the State of Arkansas.

Comments and exceptions filed on behalf of the SPSC expressed support for adjusting the Class I price surface in each of the three marketing areas but asserted that the price adjustment increases adopted in the tentative partial decision will not sufficiently increase local milk production in the three marketing areas. SPSC reiterated a number of positions given in record testimony and brief: 1) lowering the touch-base standards will have a negative impact on milk prices and production in the three marketing areas, 2) changes to the transportation credit balancing fund provisions will encourage unnecessary milk movements to the detriment of producer mailbox prices in the Appalachian and Southeast marketing areas, and 3) milk produced on farms located far from the marketing areas will seek to capture higher transportation credit payments by taking advantage of the lower touch-base standards along with the extension of transportation credit eligibility on the full loads of milk.

Comments and exceptions filed on behalf of Dean/NDH expressed opposition to the tentative partial decision by reiterating its positions given in record testimony and post-hearing brief: 1) USDA has deserted utilizing a nationally coordinated pricing surface for Class I milk; 2) current economic conditions demand a nationally coordinated price surface; and 3) abandonment of a nationally coordinated Class I price surface does not follow the requirements of Administrative Procedure Act (APA) or the Agricultural Marketing Agreement Act (AMAA). Similarly, Dean/NDH comments and exceptions also continued to criticize the method used to create the Class I price surface adjustment.

Comments and exceptions filed on behalf of the MIF reiterated its opposition given in record testimony and post-hearing brief to adjusting the Class I price surface in the Appalachian, Southeast, and Florida Federal milk marketing areas and USDA's conclusion to implement the proposed changes on an interim basis. According to MIF's comments and exceptions, increasing Class I prices and adjusting the Class I price surface will not solve the problem of covering procurement costs of fluid milk. MIF asserted that over-order payments are already used to compensate cooperatives that bear the costs of balancing the supply and that increasing Class I prices will only increase costs for processors, retailers and consumers and discourage Class I sales.

No comments and exceptions were received regarding the proposed increase in the maximum administrative assessment for the Appalachian, Southeast, and Florida orders.

Discussion and Findings

The record of this proceeding reveals that for many years milk production has declined in the southeastern region and supplying the region with supplemental milk has demanded the sourcing of milk supplies from ever farther distances from the marketing areas. Not only has the decline in milk production been in absolute terms, but when balanced with population increases, milk production in the region has failed to satisfy fluid demands year-round.

The proposed amendments in this proceeding to the Appalachian, Florida, and Southeast milk marketing orders aim to assure an adequate supply of milk for fluid use in the southeastern region of the U.S. As proposed by DCMA, the amendments to the three marketing orders seek simultaneous changes with the aim of providing incentives for

assuring a reliable supply of milk for fluid use. The amendments integrate: 1) higher regulated minimum prices for Class I milk, 2) changes to assure that the revenue accruing from higher minimum Class I prices will be shared with those producers who regularly and consistently serve the region's Class I needs of the region, 3) cost savings for entities who have made the commitment to supply the region, and 4) flexibility and incentives for supplying the Appalachian and Southeast marketing areas with supplemental milk by offsetting the cost of transportation.

Class I Prices and Class I Price Surface

Adjustments to the Class I prices for the three southeastern orders continue to be proposed for adoption in this final decision and result in a change to the Class I price surface. The changes are specified in the order language. Assuming no other changes to the three southeastern orders, increasing Class I prices will continue to increase Class I prices as provided for in the interim rule and increase the value of each order's marketwide pool. The higher Class I prices also will attract milk to all locations and increase blend prices for dairy farmers whose milk is pooled on the three southeastern milk marketing orders.

The basic foundation for deriving the temporary adjustments to Class I prices begins with DCMA's identification of potential supply areas and reliance on the areas to yield the lowest Class I price adjustment based on the farthest point of milk demand. The potential supply point meeting these criteria was Wooster, OH, and the farthest demand point was identified as Miami, FL. After identification of the lowest cost supply and demand point, the distance between these two points was relied upon to determine calculated price adjustments at all other county and parish locations within the marketing

area boundaries of the three southeastern orders. The selection of Miami as the farthest point of milk consumption is consistent with recognition in the current pricing structure that Miami is the point with the highest Class I differential resulting in a Class I price designed to attract an adequate supply of Class I milk.

As the proposal indicated, the selection of Wooster, OH, (Wayne County) as a supply point is one of several that were considered by the proponents. The selection of Wooster was made after consideration of other supply points because it would represent the least-cost point from which a milk supply could potentially be sourced from locations in the southeastern region. All other supply points considered would have resulted in much higher Class I price adjustments.

The Class I price adjustment calculated for every county and parish location relies upon a mileage rate factor implemented in December 2006. This factor is further reduced by 20 percent. While this formed DCMA's basic foundation for adjusting Class I prices, it is not the proposed Class I price adjustments at all locations in the southeastern region.

The DCMA's Class I price adjustments differ from those calculated. What the proponents have described as "smoothing" of the Class I price adjustments is essentially price alignment. In this regard, it is clear that the adopted Class I price adjustments are different from strictly calculated values. The adopted Class I price adjustments provide reasonable alignment with the current Class I price surface beyond the geographical boundaries of the southeastern orders.

Similarly, DCMA's Class I price adjustments differ from calculated adjustments by adjusting calculated values to correspond to Class I processing plant locations. This establishes pricing zones that are conceptually identical to current pricing zones and

assures that similarly situated Class I handlers will have the same minimum regulated Class I prices. Providing similar regulated prices for similarly situated handlers is consistent with the requirements of the AMAA. While conceptually identical, maintaining price alignment with adjoining milk marketing orders together with pricing zones, the adopted Class I price adjustments result in price relationships that are different from those that existed at the time of the hearing. Despite criticism that DCMA's adjustments change price relationships between plants of the same ownership, the key requirement that similarly located plants have similar regulated minimum prices is maintained.

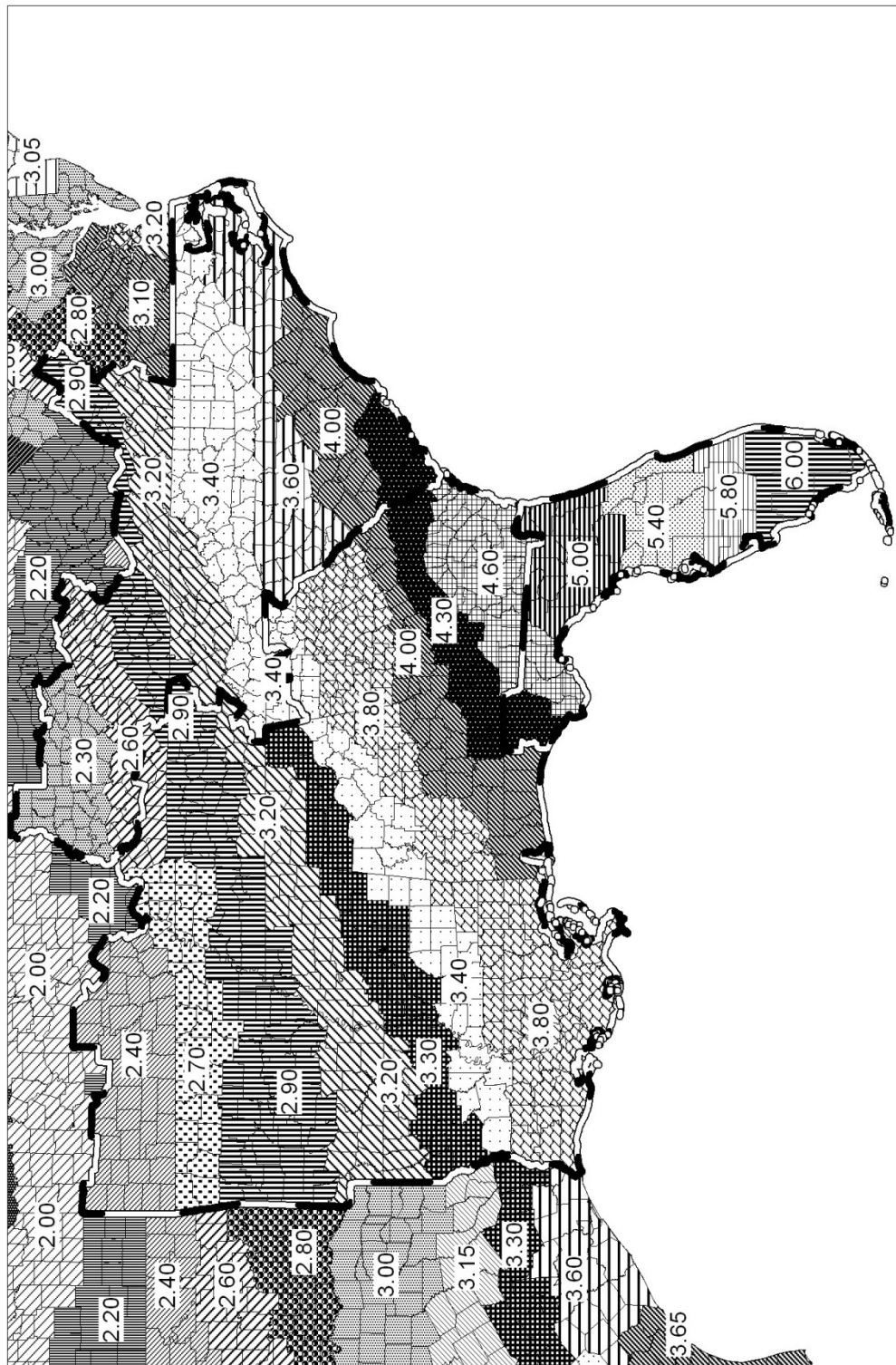
In an effort to examine both the level and the reasonableness of the Class I price adjustments that were zoned and aligned with adjoining orders, DCMA evaluated the cost of shipping packaged milk. According to the record, there are some differences between what the resulting Class I price adjustments would be under the cost analysis of shipping packaged milk. Nevertheless, the similarities between the adopted Class I price adjustment and the cost adjustment analysis of shipping packaged milk are very similar. Since the Class I price adjustment at all locations does not exceed the value of milk at alternative locations, in either bulk or packaged form, the Class I price adjustments are reasonable. Despite criticism in comments and exceptions, this final decision continues to find that this method of evaluating the Class I pricing changes forms a rational basis to conclude that the proposed changes to Class I pricing are reasonable. The adopted Class I price adjustments are presented in Figure 1. While the Class I differentials in the southeastern region are not changed in this decision, the Class I price adjustments are added to the current Class I differentials for illustrative purposes. Figure 1 provides a

graphic presentation of the combined value of Class I differentials plus the adjustment values adopted in this decision.

On the basis of a pricing surface alone, the adopted Class I price adjustments will not likely result in the uneconomic movement of milk as asserted by opponents. The adopted pricing surface better reflects the economic conditions affecting the supply and demand for milk in the three southeastern marketing areas by providing greater pricing incentives indicative of actual milk movements and the cost of supplying milk from alternative locations. The adopted Class I price adjustments result in a steeper Class I price surface that correlates with the higher location value fluid milk has in the southeastern region. The location value of milk is higher because of the cost involved in transporting milk to locations in the milk-deficit southeastern region from alternative milk-surplus locations.

Adjusted Class I Price Surface

Appalachian, Florida, and Southeast Marketing Areas



Opponents to DCMA's Class I price adjustments assert that there is no reason to increase Class I prices because all Class I demands are being met. This decision continues to find that DCMA's proposed adjustments to the pricing provisions of the three orders are reasonable and necessary. The record of this proceeding reveals that it is the cooperative member organizations of DCMA who supply the majority of the Class I needs of the three marketing areas. In making the commitment to supply the fluid needs of the markets, the supplying cooperatives have largely reduced the burden on Class I handlers to source their supply. Similarly, it is the cooperative organizations that provide the service of balancing the three southeastern markets.

Opponents to DCMA's Class I price adjustments noted that there is an adequate supply of milk to meet fluid demands. There is an adequate national supply of milk to meet the national demands for fluid milk. However, in the deficit areas of the southeastern marketing areas, there must be sufficient incentives provided by the orders to encourage the movement of milk from reserve areas to these deficit markets. In this regard, the location value of milk needs to consider local milk supplies, local demand, and transportation costs. After consideration of comments and exceptions, this decision continues to find that the adopted Class I price adjustments should provide the additional incentives needed to offset some of the costs associated with the decreases in local supply, increases in local demand, and increases in transportation costs.

Opponents criticized DCMA's Class I adjustments by identifying that other means and methods are available which would return greater revenue to dairy farmers instead of increasing minimum prices. Other changes adopted in this decision will, all other things being equal, tend to increase minimum regulated prices paid to producers. However,

these changes are founded on the very limited improvement gained from lowering the diversion limit standards of the Appalachian and Southeast orders. In light of the chronic milk deficit conditions of the southeastern region, only higher minimum regulated prices can reasonably generate the additional revenue needed to assure that the Class I needs of the region can be met continuously. According to market administrator analyses, the estimated annual increase of the Appalachian order pool for 2004, 2005, and 2006 resulting from DCMA's proposed Class I price adjustments would have been \$19.3 million, \$18.6 million, and \$18.3 million, respectively. For the Southeast order, the annual pool value increase would have been \$16.8 million, \$17.1 million, and \$17.7 million, respectively. For the Florida order, the annual increase in pool value would have been \$36.4 million, \$38.3 million, and \$39.2 million, respectively. While alternative methods such as a tightening of pooling standards will, among other things, tend to enhance producer revenue to those producers who regularly and consistently supply the market's Class I needs, this alone will not establish minimum regulated prices high enough to attract an adequate supply for chronic milk-deficit marketing areas from alternative distant locations.

Opponents expressed concern about producers in the region being involved with a voluntary producer-funded program known as the Cooperatives Working Together (CWT). CWT is a non-government program that includes a herd retirement program, which reduces the number of cows in the national dairy herd. This decision rejects this argument as it is not germane to the issues at hand. This decision is derived on the basis of record evidence which supports the adoption of the Class I pricing surface.

AMSB, in its comments and exceptions, proposed additional Class I price surface changes for certain counties in Arkansas with the aim of raising local milk production. This decision rejects adoption of the proposed increases for the Arkansas county locations for two fundamental reasons. First, doing so would not result in a reasonably aligned Class I price surface with the current national Class I price surface. Second, the proposed additional increases are based on the narrow objective of raising local Arkansas milk production. It is the purpose of milk marketing orders to set minimum prices that result in an adequate supply of milk for fluid uses. In this regard, it is not important where the milk is produced. A function of the minimum prices set by the orders is to ensure that a sufficient supply of milk will be delivered to where it is demanded. While AMSB's proposed additional Class I price increases for certain Arkansas counties would provide an even greater incentive to deliver milk to those locations, the adjustments are justified with the goal of increasing local milk production. Accordingly, AMSB's proposed Class I pricing increases for certain Arkansas county locations cannot be deemed superior to those of the DCMA proposal that clearly seeks price increases necessary to assure an adequate supply of milk from any source while also maintaining reasonable alignment with a nationally coordinated Class I price surface.

Diversion Limit and Touch-Base Standards – Appalachian and Southeast Orders

DCMA's proposed diversion limit and touch-base standards for the Appalachian and Southeast orders continue to be proposed for adoption in this final decision. The proposed changes make the diversion limit and touch-base standards of the two orders identical. Specifically, the proposed diversion limit standards are: 1) 25 percent of deliveries to pool plants during each of the months of January, February, July, August,

September, October, and November, and 2) 35 percent in each of the months of March, April, May, June, and December. Both orders' touch-base standards are amended to require at least one day's milk production of a producer be delivered to a pool plant during the month in order for a producer to be eligible to divert milk to nonpool plants.

Based on record evidence, adoption of a one-day per month touch-base standard for both orders and making the diversion limit standards of both orders identical accomplishes three important pooling standard objectives. Specifically, the changes: 1) provide a standard necessary to identify producers supplying the markets' Class I needs, 2) provide the criteria to identify the milk of producers who may be eligible for receiving a transportation credit in supplying supplemental milk for Class I use, and 3) allows milk that is part of the milk supply which regularly and consistently services the markets' Class I needs to be pooled on the orders.

Providing for the diversion of milk is a desirable and needed feature of an order because it facilitates the orderly and efficient disposition of milk when not needed for fluid use. When producer milk is not needed by the market for Class I use, some provisions should be made for that milk to be diverted to nonpool plants but remain pooled and priced under the order. The lower diversion limits adopted in this decision will likely reduce the volume of milk eligible to be pooled by diversion to a significant degree on the Southeast order and less so on the Appalachian order. Assuming all other conditions being equal, the adopted changes in diversion limit standards will result in higher blend prices paid to producers. This is a desirable outcome, especially for the Southeast order where there is the need to better identify the milk of those producers who regularly and consistently service the Class I needs of the Southeast marketing area. An

examination of the Southeast order's utilization of milk belies the fact that the marketing area is chronically short of in-area milk production to meet the Class I demand of the marketing area. This can only be the result of pooling much more milk on the order than is necessary as part of the legitimate reserve supply of milk available to service the Class I needs of the market.

The record reveals that according to market administrator analyses, the estimated impact on minimum order uniform prices of the proposed diversion limit standards in both orders would have average annual increases in uniform prices of \$0.02 per cwt for the Appalachian order and \$0.07 per cwt for the Southeast order. Increased blend prices will help to provide greater incentives to maintain milk production from current producers and provide greater economic incentives for dairy farmers located outside of the marketing area to be regular and consistent suppliers of Class I milk to these two marketing areas.

Milk diverted to nonpool plants is milk not physically received at a pool plant. However, it is included as a part of the total producer milk receipts of the diverting plant or cooperative entity pooling milk for its own account. A diversion limit establishes the amount of producer milk that may be associated with the integral milk supply of a pool plant or cooperative acting in its capacity as a handler. With regard to the pooling issues of the Southeast order, the record reveals that current diversion limit standards contribute to the pooling of large volumes of milk on the order that does not regularly and consistently service Class I market needs. Therefore, lowering the diversion limit standard is appropriate to better assure that only milk which regularly and consistently services the Class I market is pooled. Associating more milk than is actually part of the

legitimate reserve supply available for Class I use unnecessarily reduces the potential blend price paid to dairy farmers who regularly and consistently service the Class I needs of a marketing area. Not having reasonable diversion limit standards weakens the orders' ability to provide for orderly marketing. Diversion limit standards that are too high can open the door for pooling more milk on the markets than necessary. The record supports concluding that a 33 percent diversion limit for the Southeast order during each of the months of January through June and 50 percent for each of the months of July through December has not only resulted in lower blend prices harming local producers, but has also resulted in Class I utilization rates that obscure that area as a deficit market.

For the Appalachian and Southeast orders, the record reveals that since the average reserve requirements did not differ greatly over the 36 month period (January 2004 through December 2006), having the same diversion limit standards for both orders is justifiable. In addition, by having identical diversion limit standards, the blend prices paid to producers increase as milk is supplied to locations generally in an easterly and southern direction. To the extent that this diversion limit standard may warrant future adjustments, the orders already provide the market administrator authority to adjust diversion standards as marketing conditions may warrant. Given the total milk demands of the marketing areas revealed by the record, a minimum of about 12 to 13 percent of monthly pool distributing plant receipts would be needed to meet the minimum daily, weekly, monthly, and seasonal needs, as well as a modest margin for unanticipated changes in the supply and demand relationship for Class I milk needs. Accordingly, the proposed diversion standards for the orders are reasonable and continue to be proposed for adoption in this final decision.

Touch-base delivery standards define the minimum number of days of milk production each month that a dairy farmer must supply a pool plant of an order to be associated with that market and thus qualify to have their milk pooled by diversion. On the basis of the record evidence, this decision finds reason to support adopting a 1 day touch-base standard for both orders. Conditional supporters have voiced concern for DCMA's package of proposed amendments that lower the touch-base standards of the Appalachian and Southeast order because, they believe, it represents an easing of a feature of the orders' pooling standards at a time when the opposite is needed to improve producer income in the two orders. While this concern might be conceptually valid, it does not consider that the volume of milk pooled on the two orders will be appropriately restricted by the adopted diversion limit standards. In part, because the diversion limit standards of the orders are tightened, an easing of the touch-base standard can be made without fear of pooling the milk of producers who are not part of the regular and consistent supply of milk serving the Class I needs of the two marketing areas.

While diversion limit standards are a key feature of the pooling standards of an order for defining the total volume of milk that can be pooled, an argument could be made that perhaps a touch-base standard is not necessary at all if other pooling standard features are appropriately tailored. However, a touch-base standard for the Appalachian and Southeast orders remains a critical feature of both orders because some criteria are needed to identify producers who are suppliers of supplemental milk to the two marketing areas and who thereby may be eligible to receive a transportation credit.

Record evidence indicates that by reducing the touch-base standard to 1 day per month, producers, especially cooperative member producers who bear the burden of

supplying the vast majority of milk to the southeastern marketing areas, would avoid the cost of delivering their milk to pool plants when not necessarily needed. While a higher touch-base standard tends to support the integrity of the orders' performance standards, the current touch-base standards result in the uneconomic movement of milk solely for the purpose of meeting a pooling standard. The current touch-base standards of the two orders too often result in the substitution of local milk with the milk of more distant producers, thus displacing the milk of local producers supplying the market. The milk of local producers needlessly incurs the cost of being transported to more distant locations. As a result of the current touch-base standard, hauling and marketing costs are needlessly higher and the supply of milk from distant producers may still not be available to serve the Class I needs of the two marketing areas.

Despite comments and exceptions received by SPSC and AMSB and for the reasons discussed above, this decision continues to find that the diversion limit standards of the Appalachian and Southeast orders at the time of the hearing resulted in the pooling of more milk than could reasonably be considered as actually serving the markets' Class I needs. Therefore, this final decision continues to support the reduced diversion limits proposed by DCMA. Additionally, the lowering of the touch-base standard, in light of the tightening of the diversion limit standards, does not compromise the integrity of the orders' pooling standards. Together with the adopted diversion limit standards, a lower touch-base standard for the two orders offers operational cost savings to producers supplying the market with Class I milk while simultaneously providing for identification of the milk of those producers who regularly and consistently service the markets' Class I needs.

Until December 2006, the transportation credit balancing provisions of the Appalachian and Southeast orders allowed supplemental milk loads to be used as a platform to pool additional milk on the order through the diversion process. Official notice is taken of the tentative partial decision concerning milk in the Appalachian and Southeast marketing areas issued September 1, 2006, and published September 13, 2006, (71 FR 54118) and the Interim Rule issued October 19, 2006, and published October 25, 2006 (71 FR 62337). In discussing the need for revised diversion limit standards for the Appalachian and Southeast orders it is necessary to consider the findings of that decision.

The September 2006 decision referenced above established a zero diversion limit standard on supplemental milk supplies seeking a transportation credit payment. An important finding in that decision regarding diversions associated with supplemental milk supplies was that pooling such diverted milk would provide additional revenue to help offset hauling costs not covered by the transportation credit payments then in place for the Appalachian and Southeast orders. The adoption of a variable mileage rate factor that reimburses hauling costs on supplemental milk at a level more reflective of actual costs was found to diminish the need to seek and generate such revenue to offset hauling costs at the expense of the local producers who are regularly and consistently supplying milk for Class I needs. This final decision adopts tighter diversion limit standards, especially for the Southeast order. Together with providing for higher Class I prices, tighter diversion limit standards should result in more orderly marketing conditions. The ability to pool more milk on the orders than the amount needed to regularly and consistently serve the Class I needs of the markets needlessly lowers the blend price of producers who regularly and consistently service such Class I needs.

Transportation Credit Balancing Fund Provisions

DCMA's proposed changes to the Appalachian and Southeast order transportation credit balancing fund provisions continue to be proposed for adoption in this final decision. Specifically, these changes include: 1) Extending the number of months that transportation credit balancing funds will be paid to include the months of January and February. The month of June will continue to be a month for the payment of transportation credits if requested and approved by the market administrator; 2) Expanding the payment of transportation credits for supplemental milk to include the full load of milk; 3) Providing more flexibility in determining the qualification requirements for supplemental milk producers to receive transportation credit payments; and 4) Increasing the monthly transportation credit balancing fund assessment rate for the Southeast order from \$0.20 per cwt to \$0.30 per cwt.

The transportation credit balancing fund provisions for both orders (and predecessor orders) were established in 1996 as a result of the consistent need to import supplemental milk for fluid use during certain times of the year when local production is not sufficient to meet the markets' fluid needs. Specifically, the market administrator applies a monthly transportation credit balancing fund assessment on all dispositions of Class I milk. The assessment rate adopted on an interim basis through a separate rulemaking proceeding (71 FR 62377, published October 25, 2006) was \$0.15 per cwt and \$0.20 per cwt for the Appalachian and Southeast orders, respectively. At the time of the hearing, transportation credit payments were paid from each order's transportation credit balancing fund during the months of July through December to help offset the cost of transporting such supplemental milk for Class I use. As a result of this proceeding,

January and February were added on interim bases as transportation credit payout months effective March 18, 2008 (73 FR 14153). The transportation credit balancing funds operate independently from the producer settlement funds of the two orders. Milk from producers located outside of the two marketing areas who are not part of the regular and consistent supply of Class I milk, is commonly referred to as supplemental milk.

The record reveals that the seasonal swings in milk production lead to inadequate milk supplies for fluid use in certain months and surplus supplies in other months. In the Appalachian and Southeast orders, the summer and fall (and sometimes winter) months are generally considered those months with inadequate (tight) milk supplies for fluid use, while the spring months are generally characterized as having sufficient supplies of milk for fluid use. Transportation credits are used as a method to compensate handlers that provide supplemental milk during the tight supply months by offsetting some of the costs of transporting milk to the two marketing areas.

Prior to the interim final rule issued in this proceeding (73 FR 14153) the payment of transportation credits under the Appalachian and Southeast orders was only made during the months of July through December. A feature of DCMA's proposal seeks to extend such payments to also include the months of January and February. Record evidence demonstrates reliance on supplemental milk supplies for each order's marketing area during July through December and the months of January and February showing similar demand for supplemental milk supplies.

Declining local milk production in the southeastern region of the country is well-known and is a chronic problem. Record evidence indicates milk marketings from dairy farmers located in both the Appalachian and Southeast marketing areas (pooled on any

order) has continued to decrease since 2004. Specifically, evidence shows that annual milk marketings pooled on the Appalachian order have decreased from approximately 3.94 billion pounds in 2004 to about 3.77 billion pounds in 2006. For the Southeast order, milk marketings from in-area dairy farmers declined from 5.0 billion pounds in 2004 to 4.76 billion pounds in 2006. Furthermore, record evidence illustrates that total milk production in the southeastern states of the U.S. has declined on average almost 2 percent each year since 1986 and has decreased a total of 34.6 percent since 1986 -- from 18.29 billion pounds in 1986 to 11.96 billion pounds in 2006.

In each of the years of 2004, 2005, and 2006, the months of July through January were deficit in terms of monthly in-area milk marketings (milk marketed by dairy farmers within the geographical boundaries of the two marketing areas) being consistently less than the monthly Class I producer milk pooled on the Appalachian and Southeast orders. The in-area deficit in January for both orders for all 3 years combined totaled 8.4 million pounds. While February in-area milk marketings for all 3 years exceeded Class I demands, that surplus decreased from over 44 million pounds in 2004 to just under 14 million pounds in 2006 -- a decrease of over 68 percent.

Record evidence reveals that the months of January and February are likely to become months during which local in-area milk marketings will no longer satisfy Class I demands and the Appalachian and Southeast marketing areas will need to increasingly rely on supplemental milk supplies to satisfy Class I demands. Accordingly, this decision continues to find that expanding the transportation credit payment months to include the months of January and February for the payment of transportation credits is reasonable.

June will continue to be an optional month for transportation credit payments, if requested, to be reviewed and authorized by the market administrator.

Currently, transportation credits are paid on loads of milk at the lower of the receiving plant's Class I use or the marketwide Class I utilization. DCMA's proposals seek to change these criteria by having the entire load of supplemental milk eligible to receive a transportation credit. The major justification offered by DCMA is that the cost of transporting supplemental milk, regardless of the plant's use of that milk, is the same. This decision finds that a supplier of supplemental milk sources and assembles milk demanded by distributing plants for fluid uses, but no distributing plant disposes 100 percent of its milk receipts as Class I sales. The supplemental milk supplier does not know how a receiving plant will use the supplemental milk it receives. However, it is reasonable to conclude that plants do not seek supplemental milk supplies without first having the demand for Class I use. In other words, the need for supplemental milk supplies is fueled by Class I demands that cannot be satisfied in the absence of transportation credits. It is unlikely that supplemental milk suppliers would supply full milk loads to Class I plants if the demand for milk was not at least equal to its Class I disposition, even if it has some actual lower-valued use of milk.

The current calculation of transportation credit payments in the Appalachian and Southeast orders contain a number of features to prevent offsetting the full cost of transporting supplemental milk into the marketing areas. They also contain features to prevent the pooling of milk on the orders that do not regularly and consistently supply the fluid needs of the two marketing areas. Most important is the feature denying the ability to pool milk by diversion on the basis of supplemental milk deliveries to plants in the two

orders. Current transportation credit provisions prohibit pooling diverted milk on the Appalachian and Southeast orders on loads of supplemental milk seeking a transportation credit and this prohibition is continued by its adoption in this decision. Since supplemental milk can no longer form a basis from which to pool milk through the diversion process, it is reasonable to conclude that the marketwide Class I utilization percentage of the orders will likely increase. However, this improvement alone will not likely result in offsetting the costs incurred by supplemental milk suppliers who both assemble and transport milk to plants regulated by the two orders to satisfy Class I demands.

Record evidence reveals that the Appalachian and Southeast marketing areas incur different costs in attracting supplemental milk to meet Class I needs. In recent years, the transportation credit reimbursement on claims for the Southeast order has been prorated at greater rates and more often than those of the Appalachian order. As discussed in the September 13, 2006, tentative decision for the Appalachian and Southeast orders (71 FR 54118), the Appalachian marketing area receives the majority of its supplemental milk supplies from the northern Mid-Atlantic States. The Southeast marketing area receives the majority of its supply from the Midwest and Southwest States. The location of supplemental milk supplies for the Southeast marketing area therefore tends to be more distant from the marketing area than for the Appalachian marketing area.

The need to again raise the monthly transportation credit assessment rate for the Southeast order is in part explained by the continuing need of the Southeast marketing area to reach ever farther to source milk supplies to satisfy fluid demands. Additionally, expanding the payment of transportation credits on the entire load of supplemental milk

also will likely increase the payment of transportation credit claims. At the same time, payment of transportation credit claims will be partially offset by the adopted changes to the Class I pricing surface because the calculation for determining payment considers the change in Class I pricing values between the origin of supplemental milk and the point where it is delivered. As discussed above, the need for supplemental milk supplies is fueled by the marketing area's Class I demand.

The current transportation credit provisions provide precautionary measures such that the rate of assessments beyond actual handler claims is unlikely. The transportation credit provisions provide the market administrators the authority to reduce or waive assessments as necessary to maintain sufficient fund balances to pay the transportation credits claims. Therefore, increasing the maximum transportation credit assessment rates will not result in an accumulation of funds beyond what is needed to pay transportation credit claims.

The record supports concluding that local milk production is expected to continue declining within both marketing areas. This will result in an even greater reliance on supplemental milk to meet the fluid milk needs of the markets. Record evidence shows a constant increase in both the volume and distance of supplemental milk supplies, especially for the Southeast marketing area. As such, it is reasonable to conclude that future transportation credit claims will increase. In this regard, it is important to prevent exhausting the transportation credit balancing fund before the payment of claims on supplemental milk. Doing so is consistent with the fundamental purposes of the transportation credit provisions.

The adopted increases in Class I prices will likely alter the payout of transportation credit claims because the differences in origin and delivery point Class I prices are increased. However, adoption of expanded transportation credit payment months to include January and February, as well as payments on the entire load of milk, will tend to offset the payout on transportation credit claims resulting from the adopted changes in Class I pricing.

An increase in the transportation credit assessment rate for the Appalachian order was not requested because 100 percent of the transportation credit requests were paid in 2006 and in January 2007. Hearing record data indicates that even with adoption of the proposed Class I prices, pooling requirements and transportation credit provisions, the transportation credit assessment rate of \$0.15 per cwt in the Appalachian order should continue to be sufficient to pay future transportation credit requests.

The record indicates that the actual transportation credits paid in 2006 for the Appalachian order totaled \$3,313,590. Had the current mileage rate factor (MRF) been in effect for all of 2006, transportation credit payments for the Appalachian order would have totaled \$4,433,854, including the actual payment for January 2007 and an estimated payment for February. Analysis suggests that with the current MRF and proposed Class I prices in place, the total transportation credits paid during 2006 would have been about \$456,000 less than the actual total transportation credit payments. Using market administrator data with the variable MRF based on 2006 calculated monthly averages (\$0.044 per cwt per 10 miles), paying of transportation credit claims on full loads of milk, and the proposed Class I price adjustments, the total transportation credits paid for 2006 in the Appalachian order would have totaled \$4,073,312. This is \$360,000 less than what

would have been paid with the MRF and the lower of a plant's Class I use or marketwide Class I utilization. Accordingly, the current \$0.15 assessment rate for the Appalachian order appears to be sufficient to meet all claims even when paying transportation credits on full loads of milk delivered to Class I plants regulated by the order.

The record indicates that the transportation credit balancing fund for the Southeast order has been insufficient to pay transportation credit claims. Record evidence indicates that during 2006, Southeast order transportation credit payments were prorated to 81, 36, 39, and 64 percent of the transportation credit claims for the months of September, October, November, and December, respectively. Such transportation credit claims also have increased in number of pounds and in number of miles. Specifically, the total pounds claimed for the receipt of transportation credits has increased from 374 million pounds for July through December 2000 to 820 million pounds for July through December 2006 – an increase of 119 percent.

Increasing the maximum transportation credit assessment rate for the Southeast order should not result in an unnecessary accumulation of funds. For the Southeast order, the record indicates that transportation credits paid in 2006 would have totaled \$15,704,872 for the months of July through December and would have totaled \$18,604,872 by including the months of January and February. This analysis is based on using the same MRF of \$0.044 as in the Appalachian order analysis, paying of transportation credit claims on full loads of milk, and with the proposed Class I price adjustments. However, the assessment rate of \$0.20 per cwt falls far short of the total revenue needed to pay all expected transportation credit claims. Even a \$0.30 per cwt assessment may not generate sufficient revenue to meet all expected claims on full loads of supplemental milk.

Nevertheless, a \$0.30 cwt assessment is more likely to be sufficient to cover all expected transportation credit claims.

Determining those producers eligible to receive a transportation credit on their supplemental milk deliveries requires that the dairy farmer be located outside either the Appalachian or the Southeast marketing areas, the producer must not meet the Producer definition of the orders during more than 2 of the immediately preceding months of February through May, and not more than 50 percent of the milk production of the dairy farmer during those 2 months, in aggregate, can be received as producer milk under the order during those 2 months.

DCMA has proposed that these requirements for the Appalachian and Southeast orders be made more flexible without substantially changing the identification of milk that is not a regular part of the supply of milk to the two orders. Specifically proposed is that a dairy farmer must not be a producer on the orders for more than 45 of the 92 days in the months March through May **or** must have less than 50 percent of the producer's milk pooled on the orders during those 3 months combined. On the basis of record testimony, this change is warranted. Specifically, it represents a change that provides flexibility in identifying supplemental milk producers and may result in lower operational costs to those producers incurring the costs of supplying supplemental milk to the Appalachian and Southeast marketing areas. Additionally, prior to the interim adoption, February was a month used to determine the qualification of supplemental milk producers to be eligible for a transportation credit payment. Since this decision adopts providing for the month of February as a month in which transportation credit payments can be

made, it is necessary to redefine the months that a producer may qualify to receive transportation credits on either order.

Administrative assessment increase

The hearing record reveals that fluctuations in the volumes of milk pooled on the Appalachian, Southeast, and Florida orders can be attributed to a combination of declining milk supplies and the tightening of diversion limits in all three marketing areas. This combination can reduce market administrator revenues to a level too low for the proper administration of the orders while maintaining the mandated reserve level. The adoption of Proposals 4, 5, and 6 will create a more stable revenue stream for the administration of the three southeastern orders.

It is reasonable to increase the maximum administrative assessment rate to \$0.08 per cwt in the Appalachian, Southeast and Florida orders to ensure that the market administrators have the proper funds to carry out all of the services provided by the three marketing areas. While the maximum administrative assessment rate is increased to \$0.08 per cwt in the Appalachian, Southeast, and Florida orders, the actual rate charged will only be as high as necessary to properly administer the orders and provide necessary services to market participants.

Conforming changes

Conforming changes were made to 7 CFR part 1000.50 Class prices, component prices, and advanced pricing factors. Specifically, the Class I skim milk price and the Class I butterfat price provisions were changed to conform to the amendments adopted in this proceeding as provided for in Proposal 7 of the hearing notice. The changes made to 7 CFR part 1000.50 (b) and (c) included reference to the adjustments adopted to Class I

prices specified in 7 CFR parts 1005.51(b), 1006.51(b), and 1007.51(b). The conforming changes were presented in the partial tentative final decision (73 FR 11194) and implemented by the interim final rule (73 FR 14153).

Rulings on Proposed Findings and Conclusions

Briefs, proposed findings, and conclusions were filed on behalf of certain interested parties. These briefs, proposed findings, and conclusions, and the evidence in the record were considered in making the findings and conclusions set forth above. To the extent that the suggested findings and conclusions filed by interested parties are inconsistent with the findings and conclusions set forth herein, the claims to make such findings or reach such conclusions are denied for the reasons previously stated in this decision.

General Findings

The findings and determinations hereinafter set forth supplement those that were made when the Appalachian, Florida, and Southeast orders were first issued and when they were amended. The previous findings and determinations are hereby ratified and confirmed, except where they may conflict with those set forth herein.

The following findings are hereby made with respect to the aforesaid marketing agreements and orders:

(a) The tentative marketing agreements and the orders, as hereby proposed to be amended, and all of the terms and conditions thereof, will tend to effectuate the declared policy of the Act;

(b) The parity prices of milk as determined pursuant to section 2 of the Act are not reasonable with respect to the price of feeds, available supplies of feeds, and other economic conditions that affect market supply and demand for milk in the marketing

area, and the minimum prices specified in the tentative marketing agreements and the orders, as hereby proposed to be amended, are such prices as will reflect the aforesaid factors, ensure a sufficient quantity of pure and wholesome milk, and be in the public interest; and

(c) The tentative marketing agreements and the orders, as hereby proposed to be amended, will regulate the handling of milk in the same manner as, and will be applicable only to persons in the respective classes of industrial and commercial activity specified in, the marketing agreements upon which a hearing has been held.

Rulings on Exceptions

In arriving at the findings and conclusions, and the regulatory provisions of this decision, each of the exceptions received was carefully and fully considered in conjunction with the record evidence. To the extent that the findings, conclusions, and regulatory provisions of this decision are at variance with any of the exceptions, such exceptions are hereby overruled for the reasons previously stated in this decision.

Marketing Agreement and Order

Annexed hereto and made a part hereof are two documents – a Marketing Agreement regulating the handling of milk and an Order Amending the Order regulating the handling of milk in the Appalachian, Florida, and Southeast marketing areas, that was approved by producers and published in the Federal Register on March 17, 2008 (73 FR 14153) and on May 9, 2008 (73 FR 26513) as an Interim Final Rule and Correcting Amendments, respectively. These documents have been decided upon as the detailed and appropriate means of effectuating the foregoing conclusions.

It is hereby ordered that this entire decision and the Marketing Agreement annexed hereto be published in the **Federal Register**.

Determination of Producer Approval and Representative Period

The month of July 2013 is hereby determined to be the representative period for the purpose of ascertaining whether the issuance of the order, as amended and as hereby proposed to be amended, regulating the handling of milk in the Appalachian, Southeast, and Florida marketing areas is approved or favored by producers, as defined under the terms of the order as hereby proposed to be amended, who during such representative period were engaged in the production of milk for sale within the aforesaid marketing area.

List of Subjects in 7 CFR Parts 1005, 1006 and 1007

Milk Marketing Orders.

Order Amending the Order Regulating the Handling of Milk in the Appalachian, Florida, and Southeast Marketing Areas

This order shall not become effective until the requirements of § 900.14 of the rules of practice and procedure governing proceedings to formulate marketing agreements and marketing orders have been met.

Findings and Determinations

The findings and determinations hereinafter set forth supplement those that were made when the orders were first issued and when they were amended. The previous findings and determinations are hereby ratified and confirmed, except where they may conflict with those set forth herein.

(a) Findings. A public hearing was held upon certain proposed amendments to the tentative marketing agreements and to the orders regulating the handling of milk in the Appalachian, Florida, and Southeast marketing areas. The hearing was held pursuant to the provisions of the Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601-674), and the applicable rules of practice and procedure (7 CFR part 900).

Upon the basis of the evidence introduced at such hearing and the record thereof, it is found that:

(1) The said orders as hereby amended, and all of the terms and conditions thereof, will tend to effectuate the declared policy of the Act;

(2) The parity prices of milk, as determined pursuant to Section 2 of the Act, are not reasonable in view of the price of feeds, available supplies of feeds, and other economic conditions which affect market supply and demand for milk in the aforesaid marketing areas. The minimum prices specified in the orders as hereby amended are such prices as will reflect the aforesaid factors, insure a sufficient quantity of pure and wholesome milk, and be in the public interest; and

(3) The said orders as hereby amended regulate the handling of milk in the same manner as, and are applicable only to persons in the respective classes of industrial or commercial activity specified in, a marketing agreement upon which a hearing has been held.

Order Relative to Handling

It is therefore ordered, that on and after the effective date hereof, the handling of milk in the Appalachian, Florida, and Southeast marketing areas shall be in conformity to and

in compliance with the terms and conditions of the orders, as amended, and as hereby amended, as follows:

The provisions of the order amending the orders contained in the interim amendments of the orders issued by the Administrator, Agricultural Marketing Service, on March 12, 2008, and published in the **Federal Register** on March 17, 2008, (72 FR 14153) and as corrected in the correcting amendments issued May 6, 2008, and published May 9, 2008, (73 FR 26513) are adopted and shall be the terms and provisions of these orders.

For the reasons set forth in the preamble, 7 CFR parts 1005, 1006 and 1007 are proposed to be amended as follows:

1. The authority citation for 7 CFR parts 1005, 1006 and 1007 continues to read as follows:

Authority: 7 U.S.C. 601-674, and 7253.

PART 1005 – MILK IN THE APPALACHIAN MARKETING AREA

2. Section 1005.85 is revised, to read as follows:

§ 1005.85 Assessment for order administration.

On or before the payment receipt date specified under §1005.71, each handler shall pay to the market administrator its pro rata share of the expense of administration to the order at a rate specified by the market administrator that is no more than \$.08 per hundredweight with respect to:

- (a) Receipts of producer milk (including the handler's own production) other than such receipts by a handler described in § 1000.9 (c) of this chapter that were delivered to pool plants of other handlers;
- (b) Receipts from a handler described in § 1000.9 (c) of this chapter;

(c) Receipts of concentrated fluid milk products from unregulated supply plants and receipts of nonfluid milk products assigned to Class I use pursuant to § 1000.43 (d) of this chapter and other source milk allocated to Class I pursuant to § 1000.43 (a) (3) and (8) of this chapter and the corresponding steps of § 1000.44 (b) of this chapter, except other source milk that is excluded from the computations pursuant to § 1005.60 (d) and (e) of this chapter; and

(d) Route disposition in the marketing area from a partially regulated distributing plant that exceeds the skim milk and butterfat subtracted pursuant to § 1000.76 (a) (1) (i) and (ii) of this chapter.

PART 1006 – MILK IN THE FLORIDA MARKETING AREA

3. Section 1006.85 is revised to read as follows:

§ 1006.85 Assessment for order administration.

On or before the payment receipt date specified under § 1006.71, each handler shall pay to the market administrator its pro rata share of the expense of administration of the order at a rate specified by the market administrator that is no more than \$.08 per hundredweight with respect to:

(a) Receipts of producer milk (including the handler's own production) other than such receipts by a handler described in § 1000.9 (c) of this chapter that were delivered to pool plants of other handlers;

(b) Receipts from a handler described in § 1000.9 (c) of this chapter;

(c) Receipts of concentrated fluid milk products from unregulated supply plants and receipts of nonfluid milk products assigned to Class I use pursuant to § 1000.43 (d) of this chapter and other source milk allocated to Class I pursuant to § 1000.44 (a)(3) and

(8) and the corresponding steps of § 1000.44 (b) of this chapter, except other source milk that is excluded from the computations pursuant to § 1007.60 (d) and (e) of this chapter; and

(d) Route disposition in the marketing area from a partially regulated distributing plant that exceeds the skim milk and butterfat subtracted pursuant to 1000.76 (a)(1)(i) and (ii) of this chapter.

PART 1007 – MILK IN THE SOUTHEAST MARKETING AREA

4. Section 1007.85 is revised, to read as follows:

§ 1007.85 Assessment for order administration.

On or before the payment receipt date specified under § 1007.71, each handler shall pay to the market administrator its pro rata share of the expense of administration of the order at a rate specified by the market administrator that is no more than \$.08 per hundredweight with respect to:

(a) Receipts of producer milk (including the handler's own production) other than such receipts by a handler described in § 1000.9 (c) of this chapter that were delivered to pool plants of other handlers;

(b) Receipts from a handler described in § 1000.9 (c) of this chapter;

(c) Receipts of concentrated fluid milk products from unregulated supply plants and receipts of nonfluid milk products assigned to Class I use pursuant to § 1000.43 (d) of this chapter and other source milk allocated to Class I pursuant to § 1000.44 (a)(3) and (8) of this chapter and the corresponding steps of § 1000.44 (b) of this chapter, except other source milk that is excluded from the computations pursuant to § 1007.60 (d) and (e) of this chapter; and

(d) Route disposition in the marketing area from a partially regulated distributing plant that exceeds the skim milk and butterfat subtracted pursuant to 1000.76 (a)(1)(i) and (ii) of this chapter.

[Note: The following will not appear in the Code of Federal Regulations.]

Marketing Agreement Regulating the Handling of Milk in Certain Marketing Areas

The parties hereto, in order to effectuate the declared policy of the Act, and in accordance with the rules of practice and procedure effective thereunder (7 CFR part 900), desire to enter into this marketing agreement and do hereby agree that the provisions referred to in paragraph I hereof, as augmented by the provisions specified in paragraph II hereof, shall be and are the provisions of this marketing agreement as if set out in full herein.

I. The findings and determinations, order relative to handling, and the provisions of § _____ to _____² all inclusive, of the order regulating the handling of milk in the _____³ marketing area (7 CFR part _____⁴) which is annexed hereto; and

II. The following provisions: § _____⁵ Record of milk handled and authorization to correct typographical errors.

(a) Record of milk handled. The undersigned certifies that he/she handled during the month of _____⁶, _____ hundredweight of milk covered by this marketing agreement.

(b) Authorization to correct typographical errors. The undersigned hereby authorizes the Deputy Administrator, or Acting Deputy Administrator, Dairy Programs,

² First and last section of order.

³ Name of order.

⁴ Appropriate part number.

⁵ Next consecutive section number.

⁶ Appropriate representative period for the order.

Agricultural Marketing Service, to correct any typographical errors which may have been made in this marketing agreement.

Effective date. This marketing agreement shall become effective upon the execution of a counterpart hereof by the Department in accordance with Section 900.14(a) of the aforesaid rules of practice and procedure.

In Witness Whereof, The contracting handlers, acting under the provisions of the Act, for the purposes and subject to the limitations herein contained and not otherwise, have hereunto set their respective hands and seals.

Signature

By (Name)-----

(Title)-----

(Address)-----

(Seal)

Attest-----

Dated: February 25, 2014

Rex A. Barnes

Associate Administrator

BILLING CODE 3410-02 P

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